

THE PARLIAMENT'S RESPONSIBILITY FOR ECONOMIC DEVELOPMENT

REPORT OF THE CENTRAL AND EASTERN
EUROPEAN INTERPARLIAMENTARY SEMINAR
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MARCH 22-24, 1991



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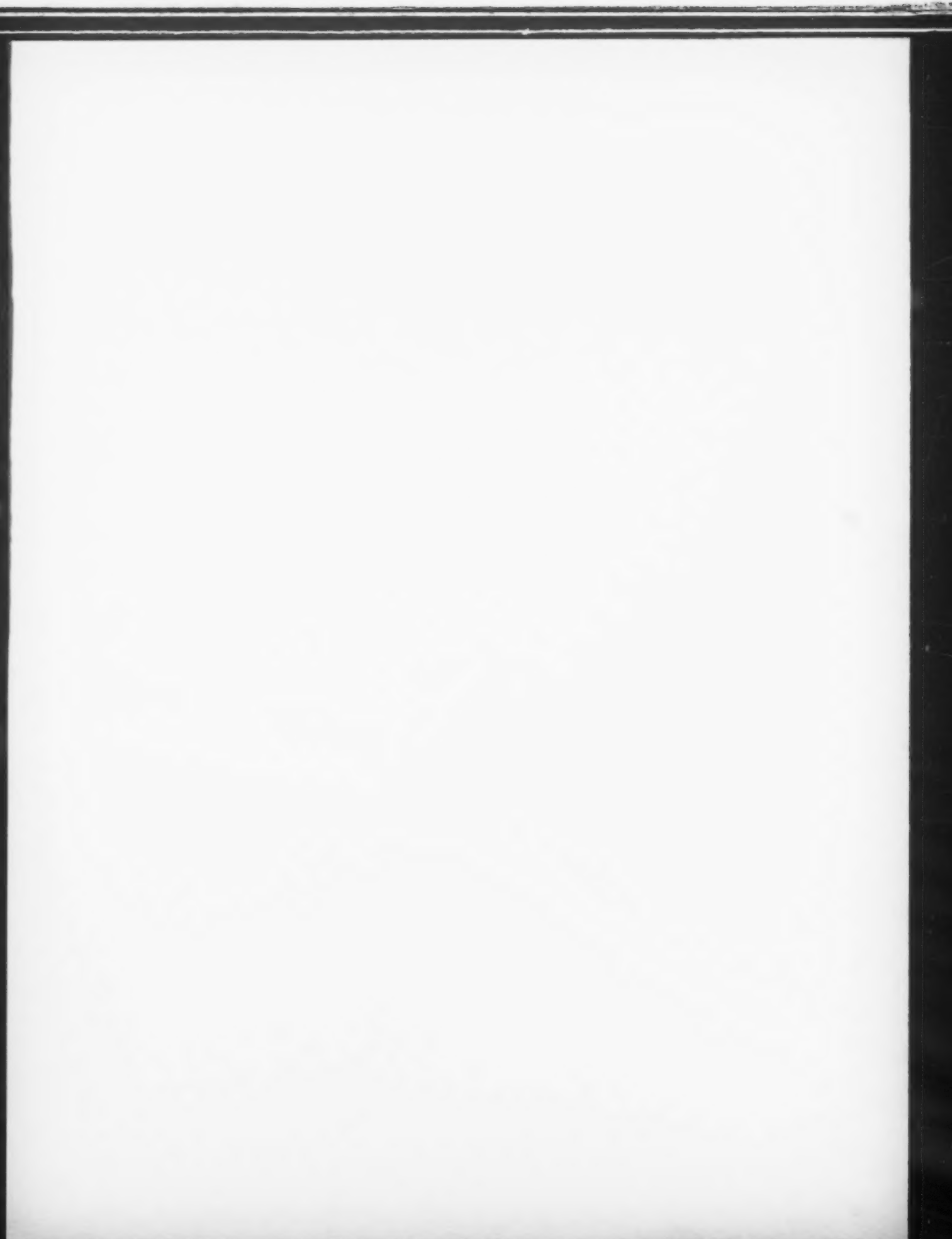
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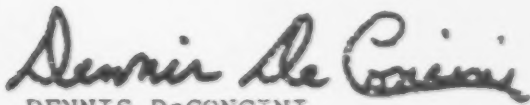
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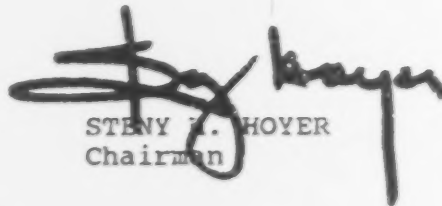
We are pleased to provide you with this compilation of papers from the Seminar on Parliamentary Responsibility for Economic Development, held in Budapest, Hungary, March 22 to 24, 1991. The Commission on Security and Cooperation in Europe cosponsored this event along with The International Foundation for the Survival and Development of Humanity, The Congressional Research Service, and the Hungarian Parliament, which served as host.

The seminar was inspired, in part, by the work accomplished at the 1990 Bonn CSCE Conference on Economic Cooperation in Europe and made possible by the positive changes which have occurred in much of Central and Eastern Europe as well as the Soviet Union. It provided a unique opportunity for parliamentarians from the region to gather with economists and other experts to explore ways of fostering market-oriented economies following decades of central planning under Communist rule. It served as a stimulating forum for an exchange of views on a wide-range of structural and monetary issues vital to this transition.

The discussions highlighted the tough choices faced by parliamentarians and others as they attempt to overhaul shattered economies. We hope that the dialogue begun in Budapest will continue during the coming years as the leaders of Central and Eastern Europe and the Soviet Union face great challenges and tremendous opportunities.



DENNIS DeCONCINI
Co-Chairman



STENY H. HOYER
Chairman



PREFACE

This unusual Budapest seminar was unprecedented in the way in which it brought together a number of diverse, but indispensable professional communities to look at Parliament's Responsibility for Economic Development in Central Europe.

In the early Spring of 1990 Program Staff of The International Foundation approached representatives of the Hungarian Parliament with the idea of assembling parliamentarians, government officials, senior corporate executives, bankers, and international economic experts in order to share their differing but interlocking perspectives on this urgent theme. This proposal was based on the realization that the fragile new parliaments of Central and Eastern Europe, grappling with complex and historic structural transitions, and very deeply concerned with the core issues of privatization, development of market mechanisms, and facilitation of effective foreign investment, could not solve their problems within the heady atmosphere of parliamentary debate alone. First, they required intensive consultation with those corporate, banking, analytical, and government communities whose expertise, influence, and actions would largely condition the success or failure of their legislative initiatives. Second, they required the comparative experience and consultation of all other parliaments and states in the region whose dilemmas and challenges were so similar to their own. Without such comparative, comprehensive, and professionally diverse consultation, the legislative efforts of any one of these parliaments were likely to be isolated, tentative, and hence all the more vulnerable.

The results of this consultative experiment were well worth the task of complex planning and organization. The richness and subtlety of the ensuing discussions are evident in the papers that follow. Plans are being developed by The International Foundation and colleagues in the parliaments of Central and Eastern Europe to establish a Standing Committee on Central European Transitions in order to continue such consultations in a series of regular specialized forums.

Much of the credit for the success of this first meeting goes to our colleagues in the Hungarian Parliament, Speaker György Szabad, Ferenc Kulin, Ivan Szabo, László Kovács, and others who not only provided host arrangements, but worked to shape the agenda and identify key participants. International Foundation staff Edward Hodgman, Rustem Khairov, and Alexander Grigoriev helped in initiating planning discussions and developing the seminar. The Hosting Committee for the seminar was made up of International Foundation Board Members (with Former U.S. Senator Charles McC. Mathias as Co-Chair and Dr. Daniel Matuszewski as seminar liaison) and representatives of the Hungarian Parliament (with Dr. György Szabad as Co-Chair) in cooperation with the U.S. CSCE Commission (Senator DeConcini, Co-Chairman) and the U.S. Congressional Research Service (Dr. John Hardt, Associate Director). John Hardt was extremely active in identifying and recruiting international economic experts for the meeting, and he and his colleague Jean F. Boone prepared both the conceptual framing paper for the seminar and this volume for publication. The framing paper

drew from an article by the same authors, "Strategies for Facilitating East European and Soviet Transformation," published by The Atlantic Council in November 1990. This paper provided guidance to the dialogue at the Budapest meeting and is the basis of the sections in the text entitled **Highlights and Commentary**. John Hardt, Jean Boone, Nancy Davenport, and Linda Kline managed the production of this publication, including obtaining selected translations. The principal figure in coordinating the complicated international logistics of the seminar and completing all final arrangements with our Hungarian hosts was the legal counsel of The International Foundation, Michael Silverman.

The International Foundation draws on a rich background of related activities in support of parliaments and economic development in countries in transition. Under the guidance of a distinguished international board of 31 scientists, corporate leaders, academicians, and public figures from 15 countries in North America, Europe, Asia, Africa, and Latin America, the Foundation sponsors and supports almost 40 innovative projects annually in areas concerned with the development of civil society and the rule of law.

The U.S. Congress is supporting the legislatures of the Central European developing democracies through the Special Task Force on the Development of Parliamentary Institutions in Eastern Europe, chaired by Representative Martin Frost, and the Gift of Democracy to Poland led by Secretary of the Senate Joseph Stewart. The Congressional Research Service of the Library of Congress, in efforts coordinated by William H. Robinson, Deputy Director of CRS, assists the congressional initiatives focused on strengthening parliamentary resources and building a legislative research capability. In addition, the Congress has approved exchange and cooperative efforts by CRS with the Supreme Soviet of the U.S.S.R. The U.S. Commission on Security and Cooperation in Europe was actively involved in the CSCE Bonn Conference on Economic Co-Operation in Europe in March-April 1990 reflecting its continuing interest in political and economic developments in the region.

It goes without saying that the leaders of the various national delegations and the parliamentary delegates themselves made the major substantive contributions through their reports and commentaries. Experts from the international organizations, banks, and private businesses brought valuable professional perspectives that made for an unusually creative mix. We are grateful to all those who took time away from their schedules to bring their comparative developmental expertise to these discussions. We look forward to continued consultation with colleagues from this group. Finally, we also are grateful to Rockefeller Family & Associates, who provided financial support to The International Foundation early in the organizing process, and to the Ford Foundation for its generous contributions to several of the sponsoring organizations in support of this seminar.

Daniel C. Matuszewski

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EXECUTIVE SUMMARY

The Parliament's Responsibility for Economic Development

by

John P. Hardt and Daniel C. Matuszewski

Purposes of Seminar

- To define the responsibility and specific influence of parliaments in the economic development of Central and Eastern European countries in transition, by bringing together representatives of the major groups whose active participation and involvement in the process of transition are critical.
- To develop a common policy framework, through discussion, that reflects consensus among the parliaments of Europe in transition. This common policy framework would be established at a time when all the transforming countries are clarifying their objectives and reorienting their legislative processes to new requirements; it would provide some general agreement on objectives and on the means available for achieving those objectives.

Broad Representation and Involvement of Relevant Policy Groups at the Budapest Meeting

The agenda included over 100 active participants representing all of the following groups:

- Leaders of all Central and Eastern European parliaments. (For the purposes of this report, Central and Eastern Europe is taken to include Bulgaria, the Czech and Slovak Federal Republic, the states of Germany in transition, Hungary, Poland, Romania, the U.S.S.R. and Yugoslavia.)
- Representatives of Western parliaments: the German Bundestag and the United States Congress.
- International agencies: IMF, World Bank, OECD, and CSCE.
- Central and commercial bankers from West and East.
- Western and Eastern industrialists and leaders of Central and Eastern European privatization agencies.
- Professional economists and experts from West and East.

Never before has such a representative group met on this agenda, producing such a constructive dialogue on their intentions and planning for economic transformation in a democratic context.

Framing the Central Issues: Consensus and Divergence

The seminar examined both the substantive economic issues now facing the European transforming countries and the parliamentary processes that might be used to establish economic programs based on broad social consensus and effective implementing legislation:

Democracy and Marketization

All participants agreed that democratization and marketization were not only complementary but interdependent. Social pacts between the governors and the governed are essential to provide a consensual basis for sustaining the necessary, albeit painful, transition. Difficult trade-offs can best be understood and supported through political debate and compromise; the parliamentary system is especially suited for this process of developing a consensus.

Nevertheless, it was acknowledged that democratization in some ways complicates the transition to a market economy. The economic difficulties experienced in the early stages of transition, often the legacy of the old system, are seen by the population as the consequence of reform, leading to resistance and disillusionment. While little concern was expressed about possible adverse effects of populism, some participants noted the problem of mobilizing the population to support and assist the economic transformation, while avoiding irresponsible political tendencies. Negative short-term income and employment effects are often resisted, even when the requirements of transformation and restructuring dictate these short-term costs.

Less consensus was expressed by the parliamentary delegations on the need for decentralization of economic policy-making and management. Local and regional government roles, especially in those countries with ethnic diversity, were not discussed in any uniform fashion. In countries with ethnic and regional divisions, the issue of decentralization is critical but was not always explicitly acknowledged. In the view of some, the legal, parliamentary process must be allowed to resolve these disputes, even if it is slow and cumbersome.

Also, the parliaments were shown to be constrained in their ability to institute market reforms by different parliamentary means. Some emphasized the need to strengthen parliamentary oversight and enforcement powers in order to ensure the implementation of laws. Others noted problems in the composition of their parliaments which inhibited the movement toward economic transformation or limited the parliament's popular legitimacy. Furthermore, the path and pace toward

democratization and marketization differ among countries depending on historical patterns, especially the presence or absence of pluralistic, entrepreneurial traditions.

Economic Programs for Transition to a Market Economy

Although the process of transition from a command to a market economy is unprecedented, the transforming countries share common challenges to be addressed in their economic programs -- in particular, creating market and financial institutions and mechanisms for private ownership. All seemed to accept in principle that their economic programs for effective transition should be comprehensive and simultaneous, rather than focused solely on monetary stabilization or any one transitional requirement at the expense of other objectives. They all accepted that a certain threshold of commitment is necessary to assure irreversible transitions. They also recognized that these kinds of comprehensive programs were necessary for Western support and aid.

However, none of the countries articulated the detailed need for comprehensiveness and the necessary threshold commitments for each element of the program. Although most participants acknowledged the need to minimize social costs where possible, few addressed the concrete problem of trade-offs among employment, growth and incomes - including those that derive from the "butter over guns" choice. Furthermore, there were differences expressed in defining the economic role of the state in the transition. While some noted the importance of government's regulatory role, most did not give adequate attention or commitment to social safety nets, medical, environmental and housing problems. Little attention in the initial stage of the programs was given to infrastructure problems, especially in the regional context.

Some stressed the need for a comprehensive and simultaneous framework of transition but with a careful working out of a professionally sound and politically acceptable process for proceeding toward full implementation.

Likewise, ensuring foreign competitiveness by improved domestic savings and investment patterns was given limited attention.

Effective Integration into the World Economy

Parliamentary delegates themselves espoused the greatest dedication and enthusiasm for early openness and integration with the international market economy. The lure of membership in the European Community seemed to reflect a desire on the part of parliamentarians to join in order to share in higher living standards. In spite of the German example, little concern was expressed over premature openness leading to wide scale bankruptcy and mass unemployment. Hungary's achievement of a current account surplus offered a prospective success story in liberalization.

Achieving currency convertibility is an important goal for all the countries, but there were clear differences in the approaches taken toward convertibility. The German situation was clearly unique; Poland's rapid liberalization was determined by the dollarization of the economy; Hungary's more gradual approach was permitted by the relative strength of its currency on the domestic market.

There was widespread recognition within the Central and Eastern European parliamentary groups that the Soviet state would have to be an active participant in this transition, that patterns of economic and trade interdependence built over the past forty years were too important to ignore, and that it would be essential to include the Soviet Union in such consultative processes regarding the design of creative and mutually beneficial approaches and solutions.

The low level of Western direct investment was not directly correlated with the slow progress in their domestic programs, including continued double digit inflation; the lowest inflation rate in the region is 30 percent in Hungary. While domestic savings was accepted as a primary source for domestic investment requirements, early availability of foreign investment is also crucial as low domestic savings rates will limit domestic investment. Many lessons of the Marshall plan success in developing successful mechanisms for regional cooperation, improved technology transfer, overall productivity and progress toward convertibility were not explicitly appreciated or acknowledged.

Though many parliamentarians emphasized the benefits to be gained from integration into the international economy, other participants noted the costs and constraints. While foreign assistance and investment is available, the level of capital flows into Central and Eastern Europe depend on progress and stability in the economic transformation of each country. It is necessary to create economic conditions in which domestic investors and entrepreneurs can thrive in order to attract foreign investors and trade, Western commentators observed.

Problems in regional trade were noted by some, but given relatively little attention by the parliaments. The collapse of the Council for Mutual Economic Assistance (CMEA), especially reduced trade by the Soviet Union and Germany in the region, has serious implications for employment and production throughout Central and Eastern Europe. Several participants urged greater coordination among the countries in transition in the effort to integrate into the international economy.

Privatization

The necessary threshold conditions of destatization, corporatization and technological restructuring were generally accepted as preconditions to dispersal of assets. The difficulty of balancing criteria of efficiency and equity in the dispersal of assets were articulated by those, especially in Central Europe, grappling with privatization laws. They seem to realize that privatization will certainly be a long process. However, the

motivation and enhanced productivity deriving from privatization were generally considered essential to success of the process of transformation.

Insufficient consideration has been given to the need for a balance between government ownership and control on the one hand and elected body oversight and administration and private ownership on the other. Areas such as infrastructure would be natural sectors for public ownership.

The rate of privatization and the openness of the asset dispersal process to foreign and domestic purchasers was a subject of disagreement. The limits on domestic assets controlled by those concerned only with short-term profit is apparently reserved for the future agenda.

Privatization is seen by all as a critical element in economic transformation, necessary for the efficient allocation of investment and increased productivity. However, the individual privatization programs differ substantially in their objectives and specific mechanisms. For some, the emphasis is simply on transferring control and management from the state to other entities; for others, the goal is promoting profit and entrepreneurship; still others focus on the need for a socially just solution. These differences reflect the difficulty of balancing criteria of efficiency and equity in the dispersal of assets and the establishment of responsible ownership.

While some noted that privatization would provide badly needed revenues for the state, other participants stressed that privatization should not be undertaken for short-term revenue goals, but to maximize national income in the long run. The rate of privatization and the openness of the process to foreign investors were also the source of diverging views.

Monetary Stabilization

The link between long-term growth and stable currencies seems to have been accepted. An independent central bank and a commercial banking system are recognized requirements in most countries. Legislation is being designed rapidly to establish these institutions of monetary discipline and financial control in Central and Eastern Europe.

However, the short-term impacts of conservative monetary policy on growth, employment and living standards are not generally appreciated; the continued tension between political leaders and central bankers in the West is not yet widely perceived or appreciated. The need to assure independence of the central bank and to develop a popular culture supporting that independence requires further attention.

Fiscal policy and revenue sharing are new concepts so far little discussed or developed. Some parliaments have already fallen prey to the attraction or proliferation of costly new programs with no matching resources from tax revenues.

Summation

The purposes of the seminar were attained by assembling a representative group for a constructive dialogue on parliaments' responsibilities in economic development. A number of general conclusions can be drawn from the discussion:

- **The parliament's role is crucial in the transition to a democratic market system.** Only with the active and effective involvement of elected parliamentarians can an efficient and equitable transition be undertaken.
- **The major issues framed for the meeting are commonly and freely accepted by the respective parliamentarians** and provide a useful basis for further dialogue within and among the groups of parliamentarians.
- **A consensus on objectives, central questions and trade-offs is evident.** However, the mechanisms and choices for attaining objectives differ within and among parliamentary groups and other involved parties.
- **The dialogue on parliament's responsibilities in economic development needs to be continued** with emphasis on specific issues and exchanges among small groups of parliamentarians. This would allow for more direct dialogue among the countries on particular shared problems, and alternatively, to focus on the specific situations and challenges faced by individual countries.

I. OPENING STATEMENTS

Tamás Szabó

Member of Parliament

Political State Secretary, Ministry for Finance
Republic of Hungary

Distinguished ladies and gentlemen, good morning. May I introduce myself. My name is Tamás Szabó, head of the Hungarian parliamentary delegation. Permit me please to first of all express our heartfelt thanks for the confidence which you have given to us in advance by sharing such a keen interest in the organization of this conference and may I equally express our heartfelt thanks to the organizers--to the International Foundation for the Survival of Mankind, and to the Congressional Research Service of the United States Library of Congress, for having assisted and contributed to the organization of this conference. The program of the conference lies in front of you, so I don't think I have to inform you about the program. May I request Mr. György Szabad, Speaker of the Hungarian Parliament, please to deliver his opening speech.

György Szabad

Speaker of the National Assembly
Republic of Hungary

Distinguished ladies and gentlemen: For the Hungarian Parliament, it is a great honor that we have the opportunity, on the occasion of this conference, to welcome the parliamentary delegations of nations who have tread on the path of transformation. It has a specific purpose--that is, to look back, to study the path of transformation which has been covered and to provide a critical analysis and assessment of the experiments which have been proceeding in a similar direction and the results of this. Also, based on the above, it is the purpose of this conference to contribute and to see that in the individual countries, and in the East and Central European region as well, the transformation should be successful. There should be a chance and the possibilities [given for] this by: assessing the various experience, concepts, thoughts and ideas, considering the characteristics of the region, the political, economic, social and moral transformation taking place in the area; considering the findings which have resulted from the studies of these areas; and considering the views of those who are observers, to recognize the advice, views, remarks and assessments of those who observe us and provide us with advice.

At a reception given for the delegations, we had the opportunity to note that this meeting, besides serving a specific purpose, offers a notable opportunity from another aspect--that is, from the time we have tread on the path of transformation, this is the meeting with the broadest multilateral participation held in this region, where the parliamentary delegations of those countries taking part in the process of transformation are present. This fact in itself is of major importance. At the same time, the real values and features will be given to this conference by the extent to which we will be able to clarify the features of political and economic experimentation which take us along similar lines but which show very different features at the same time, and the extent to which we will be able to note our successes and failures, and by revealing those, be able to provide proper assistance to one another. In this way, the best possible solution for evolution should be found on an independent basis, and we should be able to find the possible paths and methods of solutions, and use the possibilities available. May I wish to all of us that the conference we are having together now be successful and that, by contributing to these discussions, we should lay the foundations for cooperation which will be free and fruitful.

Daniel Matuszewski
Executive Director
The International Foundation

Minister Szabó, Speaker Szabad:

In the name of the International Foundation I would like to add my greetings and welcome participants in this unprecedented meeting. We are meeting at a dramatic moment of unprecedented shifts in the political economies of Europe, we are meeting in the aftermath of the cold war, in the aftermath of the unification of Germany, in the aftermath of dramatic transformation in Central Europe and we are delighted to be cooperating with you in working on issues of parliamentary responsibility for economic development at this time. The Foundation has recently formed a committee on international economic transitions and we will be developing projects with many of you in this room over the course of the next few years. We look forward to these discussions as setting an essential baseline for ongoing review of our common problems.

One thing we have found in talking with our parliamentary colleagues over the last few years is that many of these discussions on legislation and the responsibility of parliaments for economic reform cannot take place in a vacuum. They must take place in consultation with government leaders, with business leaders, with leaders of banks and great corporations across the region. In talking about transitions to market mechanisms, to patterns of privatization, and to attractive patterns of foreign investment and joint venture, you must bring all of these communities into the room to share a rich set of differing perspectives on these problems.

In bringing together representatives from some 16 countries in Western Europe, Eastern Europe, Central Europe, North America, South America and Asia, we are delighted to initiate a process which we hope will bring greater attention to the urgent common agenda made up by this evolving set of challenges. The issue of emerging interdependence is by now almost universally recognized, and we are pleased to welcome here today, in recognition of such interdependence, representatives from countries as far away as Korea, Brazil, and Egypt. I extend my welcome and best wishes to all participants and observers in these landmark discussions.

II. PARLIAMENTS AND ECONOMIC DEVELOPMENT

Highlights and Commentary

The countries of Central and Eastern Europe have embarked on a comprehensive transformation of their political and economic systems. While democratic and market systems may promise freedom and prosperity in the long term, the period of transition involves high economic costs, difficult political trade-offs, and urgent human and institutional demands. The newly elected governments of these countries face the daunting tasks of developing policies and creating new institutions which can produce political and social stability, economic growth, and integration into the international economy.

In navigating the transition, the popularly elected legislatures of the region will play a critical role. Regardless of differences among them, all of the parliaments will have some responsibility for establishing the legal and regulatory framework for economic activity, deciding budget allocations, and providing effective mechanisms for administrative oversight. Through these two functions, legislation and oversight, parliaments can concretely influence and even determine the conditions for economic development.

More broadly, the parliament, as a representative institution, provides a crucial link between the administrative organs of the state and the population. This linking function is especially important in a time of comprehensive transformation, when strategic choices must be made affecting basic political and economic arrangements in society. In fashioning national policies, the legislature offers a public forum for debate in which the opinions of society can be voiced. Likewise, through discussion and amendment of policies put forward by the executive, the legislature can give government programs popular legitimacy and authority, strengthening the prospects for their successful implementation.

Given the difficult economic transition now underway in Central and Eastern Europe, the consent and involvement of the public will be a necessary foundation for the success and sustainability of economic reforms. It is through these representative parliamentary institutions, principally, that such consent and participation can be expressed and a social pact in support of comprehensive reform programs can be established.

Each delegation, in its opening statement, reflected these general concerns. All are working to establish the parliament's responsibilities and to define, through legislation, a new relationship between the state and the economy. However, the specific character of the emerging relationship differs among the countries in transition, as each country seeks solutions compatible with its own political and economic conditions. The nature

of these differences among countries became clearer in the subsequent sessions focused on narrower topics.

* * * * *

Árpád Göncz
President
Republic of Hungary

Ladies and Gentlemen, Participants of this Conference, Dear Guests:

In my capacity as Head of State of the Hungarian Republic, I would like to extend to you my personal welcome. I hope your stay here will be both enjoyable and useful. The region we share--the eastern part of Europe--deserves to move closer to the western hemisphere. I hope that our conference, dedicated to the role of the parliaments in economic development, will contribute, however little, to this movement. This is my sincere wish for all of our neighbors in the region and that the words West and East cease to denote qualitative differences or rich and poor relatives, but only what they were originally meant to mean: points of the compass.

Ladies and Gentlemen,

Having discharged the more pleasant part of my duties, to welcome you, I would like to fill the rest of the time allotted to me with some work. I would like to say a few words about separation of legislative, executive and judicial powers, because it is clear that we can reach our common goal, rebuilding and revitalizing our troubled economies, only in the framework of a democratic, constitutional state.

"The idea of separation of powers somehow evokes the spirit of the 17th-18th century," István Bibó, one of the most important Hungarian political scientists of this century, wrote 44 years ago. "There are two elements combined in the idea of separation of powers: the effort to describe, classify, systemize, and understand the manifestations of government; and the effort to guide government activities in the proper direction: toward a moral, practical, progressive..., in other words, appropriate structure."

Here and now, however, this is not a theoretical question but a real-life issue. During the past century, the Eastern-Central-European and Eastern-European regions traveled a road different from the western part of the Continent. During the dead-end experiment with Leninist socialism, the separation of powers went no further than a declaration of intent. In reality, all power was concentrated in the hands of the party, while the legislative, executive and judicial branches were relegated to pro forma

functions following dictated interests and values. The results are known: pretentious, but unjustified laws, ruthless and bureaucratic execution, and thousands of mock trials followed by almost complete economic, social, political and moral collapse. During the same period, the better-functioning part of Europe flourished thanks to the unbroken chain of liberal democratic institutions. A freely elected legislative body, based on the sovereignty of the people, functioned in that part of Europe. The existence, in the legislative body, of an opposition ready to take over the government was natural, and so was freedom of assembly, press and thought, freedom of political organizations, as well as the independence of the courts and some kind of judicial control of government activities. The essence of separation of powers is to reduce the danger of concentration of power as well as a modern, service-oriented conceptualization of government functions ensuring that their execution is effective. Toward the end of his life, István Bibó regarded this chain of institutions inherent to liberal democracy as "the most important invention of the European people." He added that "aside from European music, this is perhaps the only idea not discovered by other cultures."

Ladies and Gentlemen,

For our region this is an era of transition. The individual countries are attempting to leave Lenin's dogma behind and return to the road of democratic states of law according to their historic traditions, current conditions and internal social impulses. After years of the one-party system, they are tasting the elation of political pluralism and after so many times of just voting, the ecstasy of elections. The legislature has to enact a huge number of new laws to ensure the political and economic transition. The government (the executive power), accountable to the elected parliament, must be up to its tasks resulting from the new legislation in spite of the internal chaos, the backward-pulling forces, the social and political tensions. The judicial institutions, such as the Constitutional Court in Hungary, have now been given the power to stand guard over constitutionality, lawfulness and equal rights of government and citizen, with full independence from the other two branches, ensuring, at the same time, that no concentration of power takes place in either the legislative or the executive branches. This is a real danger, especially regarding the executive branch, as proven by history and even by certain tendencies in the present.

In our country, we date the symbolic beginning of the transition from October 23, 1989--the proclamation of the Hungarian Republic. As a result of the modifications made in the Constitution since then, the Hungarian Constitution, the basic law of the Hungarian Republic, is now suited to ensure the transition. It clearly sets forth the separation of powers in order to prevent the concentration of power, and it has created the conditions for controlling and guaranteeing the proper operation of government. Our constitution states that "in the Hungarian Republic, all power belongs to the people exercising sovereignty directly or through their elected representatives." Accordingly, "the Parliament is the supreme governing and representative organ of the Hungarian Republic." The Parliament elects the President of the Republic, "who is the symbol for the unity of the nation and oversees the democratic operation of the government

structure"; thus, "the Government is accountable to the Parliament. It must report regularly to the Parliament on its work."

The multiple and significant authority of The Hungarian Parliament and the powerful executive resources of the government carry the risk of concentration of power, as well as the risk of unsettling the balance of powers. This is what the judicial power, the Constitutional Court in particular, must prevent, according to our Constitution, through the constitutional review of the statutory provisions. It would be an important step in establishing this third power to introduce, if possible, administrative courts, which would enable the citizens to become equals to any government office, in order to eliminate the fear of unfair and often demeaning treatment by the authorities and by the bureaucracy prevalent in our region. This would help the Hungarian people become citizens in the real sense of the word.

The President of the Republic, the modest "fourth power" with limited authority, acts as a balancer, enforcing separation of governmental powers. In this capacity I was involved in dissipating the stormy clouds in October 1990, on the occasion of the "taxi drivers' blockade" and in paving the way to a national consensus.

Finally, I would like to acknowledge the power of self-government as an independent, fifth branch of power representing further refinement of the power structure. Its authority extends only to activities of self-government; thus, unlike the legislative and executive branches, it has not even a theoretical opportunity to concentrate power in its hands.

Finally, I would like to note that exercising power in a democratic way, based on the separation of powers, means controlled exercise of power in today's Hungary. The objective of separation or division of power is not to isolate the elements of the government structure by making them completely independent from each other, but to let them operate each from its own base toward cooperation based on mutual influence and control. This is what makes me believe that Hungary is on its way to a democratic state of law, which is bound to create a fertile political ground for a flourishing economy.

Thank you for your attention. I wish you a successful conference, which should help us reach our common objectives.

György Szabad
Speaker of the National Assembly
Republic of Hungary

In ten minutes it is rather difficult to sum up this subject [of the role played by the parliaments in the transformation of the economy]. It is so extremely difficult a task that as a motto I have tried to sum up the essence of my paper in a single sentence. What I found as a suitable sentence for this purpose is this: This problem requires stabilization; it requires dynamization. If I want to elaborate on this further, I would say it requires that the state of law should be stabilized. It requires that the economy should be ready for dynamization, that the economy should be dynamized. And that the forces and powers inherent in societies should be channeled in the proper direction. This may seem to be a simplification in the true sense of the word, nevertheless, the limited time frame which is available for me and, to some extent, the problem itself, would force the speaker elaborating on this subject to try to produce a square out of a circle. It would also force the political power in a similar sense to approach this problem in a similar way, political power which has tried to implement these aims.

We have arrived in a different phase, having seen that the command systems have come to an end here in Central and Eastern Europe, which was the result of an historical turning point. After this, we have been given an opportunity and we have recognized a necessity at the same time, based on which by every possible effort we are trying to form our powers, our society, our economy. We are trying to shape the economy by channeling all these factors and forces in a new direction to provide evolution of the nation, of the society, of the economy; to lift them, to remove them, from the conditions in which dictatorship and naive attitudes, stupidity, and mistaken calculations of power were dominating.

The President of our Republic has told you rather a lot about the Hungarian constitutional endeavors and efforts, the purposes of Hungarian constitutional activities and he also has referred to the part covered in this respect. When trying to indicate the different phases of this development, may I note that the turning point which took place in the autumn of 1989 indicated the borderline of a phase of development. This phase of development was characterized by tendencies in which the political forces, the reformer groups of the former system and those in favor of renewal, were able to reach an agreement at the roundtable conference in the autumn of 1989. This agreement produced an entirely new situation. This was the platform from which the turning point became possible. The turning point became feasible for the forces of the nation who became free and this actually took place. The turning point appeared on the occasion of the free elections held in spring 1990 and, since May 1990, the forces of the new parliament have acted in this direction as well.

This parliament has drawn up a very clear direction. The parties have different concepts and, in many respects, these different concepts have been integrated by the

parliament. Thereby the parliament expressed the recognition that there was a need for change in the state structure [in order] to be able to establish the necessary preconditions for a social and economic transformation. Correspondingly, in keeping with the original functions of the parliament, the parliament's mission was restored. In other words, based on the principle of democratic majority, procedures were implemented and legislative activities, in accordance with these procedures, were placed in the hands of the parliament. The classical set of tasks to supervise the power of enforcement was also given to the parliament. Implementing the major criteria of this approach, the scope of tasks and responsibilities for the executive power was identified. Their obligations to the parliament were identified too, and these made it possible that there should be a mutual approach, working together on a mutual basis, on the supposition of cooperation between the parliament and the executive power. That is, a mutual dependence was established on this basis.

Due to the fact that my paper has to be short, I am not going to give a full list of the events. It is sometimes not in keeping with the order of dates, but I would like to point out the most important events. Partly restoring, partly modernizing its inherited traditions, the parliament reached over the commanded solutions of the dictatorship. The parliament established the basis for the restoration of the democratic system of self-government because the parliament considered that this was a necessary precondition for having a democratic state structure which in effect could provide and receive incentives from and to legislation and implementing democratism up to the possibilities available, exhausting these possibilities they should operate. Establishing these conditions the president of the republic talked about this. The reform of legislation was carried through and the third branch of power was made independent. Independence was created for this third branch of power, noting, at the same time, that the organization of judges and their upper strata became dependent on the parliament. To be more precise, they were appointed to their positions on the basis of elections at the parliament. For example, the constitutional court was elected by the parliament and thereby personal appointment was made on this basis. [This was also true] In the case of the head of the Supreme Court, and in the case of the attorney general. Thereby, in harmony with the basic principles of a democratic parliamentary state structure, we established all these required institutions. Having done so, we have provided all the possibilities for launching activities within the scope of the parliament. Particularly, legislative activities were started, the major purpose of which was the economy itself. Legislative activities covering the economy and covering the aim to liberate society were started up.

May I just point out a few cases, a few phenomena and factors which I couldn't say were all completed in the past. These are steps which we have started to make. These indicate tendencies and processes which we have started, and these are activities which are part of the major tasks of parliament which we face today. Partly, I would like to classify those in keeping with the category of themes and I would also like to refer to the various dates of legislation.

The legal aspects of ownership we would like to sort out based on the consideration that private ownership should be the focus of attention. Parallel with this, nevertheless, we would like to provide opportunities for clarifying legislative activities regarding state ownership, co-operative ownership, and community ownership. Distinguishing among various forms of ownership and changing from one form of ownership to another, transition between the two should be facilitated and made possible by items of constitution. This is the major scope of problems that the parliament has been dealing with and, within this subject area, particular attention has been paid to privatization as a necessary dismounting of the former state ownership which was imposed on the system. That is, we would like to channel back to the former types of ownership by providing the legal basis for those.

The next set of steps which the Hungarian Parliament has been considering is the following. To facilitate the mobility of capital and the accumulation of capital requires conditions which have to be regulated properly. These are the items that we deal with in harmony with the previous subject, so the two are not isolated from each other. Consequently, we make it possible for the mobility of the capital within the country to become free from the paralyzing binds and links. With due guarantees, its capital should be able to penetrate in this country and capital penetrating in this country should be deployed and located safely, that capital should be functioning properly based on the international norms and standards recognized on a general basis. When providing for these conditions, it should become possible that the capital should have an entirely free mobility in the country--not only for foreigners because essentially we can say foreign capital can have a free mobility in the country--but a similar approach should be implemented in the case of Hungarian capital, too, by providing legal basis for Hungarian capital as well.

May I just refer to a few other points because the clock seems to rush forward all the time. We have to provide free conditions for competition. We have to have a free competition. Mobility based on the principle of equality should be implemented for the parties contributing to the various activities on this basis because they should be able to operate on the basis of equal legal conditions and moral requirements would have to be implemented in the market too. These are approaches which are to be implemented by all the contributing parties in these areas. And last, but not least, we also have to provide, create, or make the conditions available for education and training, for free communication. We have to make the necessary conditions available. We have to provide for free chances for intellectual activities, for free flow of knowledge, to provide proper conditions for research, for scientific activities. We have to have a free approach and a free mobility among the areas of science, research, education, and economy, to raise those forces and to provide chances for those parties, for those people, who are able to promote political democracy, a free economy, who are capable to use the freedom provided for them by free competition.

And there is another further condition which is part of the period of transition and we have to use this too. The period of transition takes place under very difficult

conditions because it is not simply a flat, smooth area on top of which we try to construct something. This area has suffered several disasters. There are pillars which are deteriorating, almost collapsing, which we have to remove before we have a free space, a free plot for construction. And the efforts, the investment made here will not produce benefit right away. Therefore, often the society feels that democracy makes them pay the bill of dictatorship. And under conditions like that, there are two factors of major importance that are needed. One of them is that democracy in its fully developed shape has to be understood by the people. There are several examples that people understand the true character of democracy. And also people have to understand their assistance, their contribution, their help is required to make this period of transition successful. If this is done, then there will be a smaller amount of shocks, the transition will be smoother.

The apostles of democracy declared centuries ago, they have noted these days, too, that democracy is one and indivisible. Democracies have to rely on one another. This also means that the arsenal, tools, and means and methods owned by democracy are not only methods which provide mercy and help, but they should be used to assist the progress of democracy, the involvement of democracy. Living through our sufferings everyday, this has to be recognized by the people to see that this is something beneficial. This serves their interest, but with their contribution this can be functioning. And consequently, for us, for them, it becomes possible--we who quite frequently were mocked by being so slow and some people criticized us because they supposed that we were careless. We were poor in our intellectual capabilities they said. They claimed that expertise was lacking in our case. At the same time it only seems to be slow, the way we act. We try to pay attention to the motives of democracy when making the necessary steps so that we should use the energy inherent in the nation, in the peoples. We would like to encourage them to use this energy. We would also like to channel their energies and forces so that their energy should not be used to support the irresponsible actions of the irresponsible politicians trying to produce a flood by breaking through the dams of energy.

To avoid a situation like this, we would like to have a safe transformation. The Hungarian Parliament, in order to achieve this, in order to contribute to this, has adopted about 160 bills, decrees, items of law, modifications and items of legislation of various levels. You may say that this is just a small number. And you could rightly say that not all of them are masterpieces of law. Perhaps none of them are masterpieces in this sense, but we sincerely hope that they can be and they are useful tools so that perhaps, not today, not yet, can we wear lacquer shoes, shiny when walking along a shiny promenade. Perhaps we wear wooden clogs when walking there. We try to avoid the pebbles tilting but we try to cover these spots and we would like to proceed towards democracy to arrive there. We have accepted this task and it is our intention to implement this as long as we cannot see better ones to replace us.

I believe that in all these democracies, solutions will emerge from which we will learn on a mutual basis, in the interest of all of the nations, and for the benefit of all the

nations. We sincerely hope and we are convinced that this region can be raised to a truly high level, only based on a common will and wish, on the basis of a mutual cooperative approach both in the economy and the political life based on a common will.

Helmuth Becker

Vice President of the Bundestag
Federal Republic of Germany

It is a great honor and pleasure to be here today as guests of the Parliament of the Hungarian Republic. We would also like to thank the Foundation very much.

The Republic of Hungary has played a decisive part in a decades-long political, military, and economic confrontation. In many respects Hungary has had a pioneering role in the liberalization process of the Eastern European nations. We Germans, especially, feel quite particularly indebted and grateful to the Hungarians, who, by their courageous actions opened the door to freedom of movement for all Germans and hence for German unity.

With the constitutional reform and the first free elections in spring of last year, Hungary's fight for freedom was finished, and in a way that--in contrast to many other nations--was conspicuous not for its upheavals, but rather for evolution and orderly acts of legislation. If one should ask why this was so, one comes up against the trail blazing part your country has played for so many years in bringing about liberal political and economic reforms in the eastern part of Europe.

In these times of profound change and historical anticipation, it is important that we secure what we have attained and continue along the path on which we have so successfully started. High priority must be given to economic transformation.

With the economic reforms, Hungary set course for an economic idea which meets the needs of the citizens much more fully than a centrally directed socialistic economy. The social market economy proceeds on the idea that the principle of freedom of economic activity is tied to the principle of social equilibrium. The social market economy creates the prerequisites for "welfare for everyone" through its high efficiency; it counterbalances from a social standpoint the /sometimes brutal/ effects of /ruthless/ commercial activity. For this reason, it was rightly described by its initiators in the Federal Republic as a third way between unbridled liberalism and socialism, between a pure market economy and a centrally directed economy, as a synthesis of freedom guaranteed by a government based on law and welfare-state ideals, such as social security and social justice.

Parliament has the important task of creating a stable framework for law and order. The economic order to be established hereupon is theoretically open as far as its concrete shape is concerned; the results cannot be predicted in detail, as the actual shaping of economic life is determined largely by the citizens. This stands in major contrast to the determinism of socialist social orders. This openness makes any kind of prognosis difficult and contradicts the valid need of many people for security. It cannot answer the question "where and how am I going to be living and working tomorrow? Or ten years from now?" For this reason during the transition phase from a centrally directed economy to a social market economy there will be problems of acceptance which must be overcome.

A liberal constitution places maximum restraints on government while granting the citizens maximum freedom. In spite of this, any government is almost obligated to intervene in the economy for reasons of social welfare: the government is responsible for guiding the economy. Legally restricted in shaping its economic policies: this is the great parliamentary task during this period of radical change. Parliament must, in the final analysis, decide on the relationship between the market and planning, between the economy and the government.

The problem of what the right economic system should be is an old one, and has acquired new significance in light of recent developments in the member countries of the de facto no-longer-extant Council for Mutual Economic Assistance. No one would contest that "excessive" state intervention--and in more than just their economic life--has paralyzed their economies. On the other hand, it is precisely because of their desolate economic condition that these states are now faced with a real challenge. No one can offer any patent remedies as to how economic restructuring should best be accomplished. We cannot even call on historical experience, because, in the history of these countries and nations, certain market sectors have been liberalized again and again, but not whole economies. That is why even in your countries there are sound and controversial arguments about what steps to take first. I really must confess that even in the Federal Republic there is disagreement about the way to bring living conditions in both parts of Germany into alignment. In spite of all contradictions, our goal is clear: broad personal and economic freedom while taking the citizens' welfare concerns into account.

No society can remain stable over the long term if its economy is unstable. Good economic policies must walk a chalk line: if they make the economy dynamic, then they will also set loose the forces of social tension as well. If they emphasize maintenance of the status quo, then deficits and mismanagement will cause political unrest. A functioning economy and a stable society are mutual prerequisites. We will either be successful in achieving both, or both will fail in the long run. Increasing unemployment and social distress may seriously jeopardize consolidation of the new democratic structures. The transition from a centrally administered economy to a social market economy can succeed only if both the political and economic restructuring process is carried out responsibly.

The Republic of Hungary has already passed these critical phases and has progressed quite a way. It is more true of Hungary than of comparable countries being restructured that democratic renewal and economic renewal are travelling along parallel, synchronous, and fairly orderly tracks. With its fundamental renovation of government institutions and economic policy, Hungary has, in a very short time, overcome its centralized bureaucratic system from within. Of signal importance: the new constitution, a freely elected parliament, a democratically inclined administration, and legislation that in matters of economic policy emphasizes decentralization, private initiative, and the market economy, that is opening Hungary to the West, and is seeking to be incorporated into the international division of labor.

If you would permit me, before I go into the fundamental possibilities open to a parliament in restructuring the economy, I would like to point out one important role parliament might play in a free society; one which goes beyond the classical tasks of legislating and controlling the administration.

I am not in any position to give advice or make suggestions. It must be realized that every country makes varying use of the possibilities open to it for intervention. Even Hungary will go its own way, one which is appropriate for Hungary. We Germans have had two, in today's view radically different, experiences with transforming of an entire economy: once in the post-war period and, more recently, during German reunification.

The economic experiences we had during the post-war period must, on the whole, be considered positive. Ludwig Erhard and other initiators of the social market economy enjoy high esteem today in the Federal Republic. I am, however, of the opinion that we could make only partial use of the practical knowledge we garnered at that time, and only with reservations could this knowledge be transferred and applied at the present day to other countries. But if I may draw up a short balance sheet: it has been shown that a market economy is capable of releasing a high degree of economic power. But the same is true here as elsewhere: although a policy of public order */Ordnungspolitik/* points in the right direction, everyday reality cannot be dealt with in terms of pure and unsullied doctrine. A responsible economic policy must take into consideration the social classes that will be heaviest hit by liberalization, restructuring, cutbacks in subsidies, and absence of price controls. One must act pragmatically and always remember that, in the final analysis, we are dealing with the welfare of human beings.

Even the comparatively small amount of practical knowledge we acquired as a result of German unification is not really applicable to other countries. From an economic viewpoint, the five new federal states are having to deal with a radical liberalization of trade together with a drastic upward revaluation. Liberalization of this kind, from a situation where there were high trade barriers, inevitably involves a high risk to protected industries and jobs. Even the International Monetary Fund, which normally advocates drastic liberalization, would recommend cushioning the shock by devaluing the currency in such cases. This could no longer be done in the former GDR because

the GDR currency had been abolished: and here is a fundamental difference between the former GDR and all the other countries of Central, East and Southeast Europe which makes transfer of the practical knowledge we have gained almost impossible. So, if I seem rather stingy with recommendations, nevertheless, I would like to emphasize: the path we have started out on, leading from economic liberalization to the social market economy, is the right one.

I say this aware that the Hungarian economy is having problems right now. Debt and inflation are rising, and privatization is proceeding only with great difficulty. We realize, now that the initial euphoria has died down, that any improvement in economic conditions, even if laid out in carefully considered steps, takes a long hard time. But there is no need to lose heart. Hungary is now becalmed in what are probably unavoidable doldrums and once these have been got through, there will be renewed successes to celebrate. In this connection, I would like to mention two encouraging points: one involving domestic economy and one involving foreign trade. In Eastern and Central Europe there are 300 million people who want to satisfy their desires for consumer goods, which can be procured for the most part only domestically or from the near neighboring countries. In addition to the growing importance of the private sector, Hungary's comparatively high degree of integration into the world economy gives occasion for justifiable hope. More and more Hungarian companies have established themselves on the world market and will be able to expand their positions there. Moreover, Hungary is opening its markets for foreign investors, who will invest in Hungary largely because of the opportunity to use the Hungarian infrastructure, among other things, as a springboard to other economic partners in East and Southeast Europe. There is no question that the West will have to help.

Mikolaj Kozakiewicz
Speaker of the Sejm
Republic of Poland

Mr. Chairman, Ladies and Gentlemen,

Let me express my conviction that Budapest is a splendid place for a seminar aiming to evaluate the functions and roles of parliaments in the economic development of our countries. Hungary, Poland, and the remaining post-communist states have entered the difficult path to market economy. Our Polish path, as I can speak responsibly only for my own country, resembles a line stretched across an abyss, a line an acrobat must walk to get to the other side. It is not easy, but it is possible. However, there must be a safety net to secure the success of this difficult undertaking. I consider good economic legislation to be such a safety net guaranteeing the success of our economic transformations. Such legislation will indicate the direction of these transformations and help us in placing them within a desired, yet not restraining, legal framework.

It is not always easy, as you very well know, to find the ideal balance between pure economic regulations resulting from the spirit of a free market economy on the one hand, and the well-justified expectations of the society for quick improvement of the standard of living, on the other.

Our experiment is an unprecedented one. Abandoning the totalitarian system--I refer here to both economy and politics--requires truly surgical precision. The instruments for the operation must be supplied by the parliament.

The tenth term of the Polish Parliament operates at a period of radical transformations of the Polish economy, and that economy is in a deep crisis. These two factors--each in a different way--determine the work of the Parliament in the field of economy. Doubtlessly, therefore, both the Parliament and the Senate concentrate, above all, on creating new economic legislation. In a period of barely eighteen months the Parliament passed 162 laws, most of which are fundamental for the economy. Furthermore, a large number of existing laws have been amended.

The main subjects of the new regulations were related to the functioning of enterprises, the tax system and the budget law. Particularly significant were the law on ownership transformations in the Polish economy, the laws on insurance and employment, certain laws only indirectly related to the economy, but addressing important social problems, for example the Law on Social Welfare, and, finally, extremely important, the laws dealing with the budget. The present House changed considerably the proceedings of work on these laws. The extent and the amount of analytical work has grown.

The fact that the Parliament's attention is concentrating on the creation of new legislation influences obviously the proceedings of work on these laws. It also has its impact on the Parliament's other duties in the field of economy. We must frankly admit that the legislative proceedings are often carried out in haste. We must frankly admit that the Parliament has not been sufficiently able to carry out its control duties. This means that, according to our evaluation, the development of the economic situation in Poland and the realization of the government's economic programs have not been scrutinized carefully enough by the Parliament. In the course of the next few months, the Parliament should make an in-depth evaluation of the realization of the programs of economic transformation and stability. The need for such an evaluation results from the diminishing social acceptance of the realization of the very radical economic reform for which the economic and social price is very high.

The composition of the present Parliament is a very special one. It emerged from a special contract, and not from a fully democratic election. However, that does not seem to impair the effectiveness of its activities in economic matters. Therefore, it is difficult to accept the opinion heard every now and then in Poland, that the authority of legislation created by this Parliament is incomplete. This particular, contract character of the last elections results in certain special features and structures of the Polish

Parliament. The changes in the initial division of the Parliament into clubs have not ended in a clear cut division of the House into a governmental majority and the opposition minority. This has an important, and maybe even a positive, impact on the functioning of the Parliament. On the one hand, the government programs and projects receive the necessary majority in the House more easily as there is no clear-cut and organized opposition. On the other, however, the House has no majority either, to defend the policy of the government. This is not a typical state of affairs, nor a durable one. Still, the opinions about the Parliament's total incompetence and its lack of autonomy seem exaggerated indeed. The Parliament was able, also recently, to demonstrate its autonomy and its ability to make decisions, countering the opinions of various political personages and forces. This could well be seen during the recent debate on the self-dissolution of the Parliament.

There can be no doubt that the role the present Polish Parliament plays can be considered satisfactory. Our problems are not only the lack of a clear political structure (which, we hope, will emerge after the fall elections), but also the lack of necessary conditions to ascertain professional functioning of the Parliament. This is very important, particularly in the economic matters. The research and counseling bases, though developed, are still very insufficient. We also cannot ignore the fact that, after nearly 40 years of only ostensible parliamentarism, reconstruction of a party system and establishment of political elites ready for rational actions in the Parliament and on the other planes of Poland's political scene has indeed become a problem.

Certainly, this situation cannot be changed in haste. These are processes with their own, natural rhythm, and the key issue is not to hamper them with law or any "supra-legal" actions limiting political pluralism. We believe that, at present, there are very few factors in Poland inhibiting the process of shaping pluralism in the country's political system. If that judgment is correct, we are entitled to a moderate optimism about the future role of the Polish Parliament, also in economic affairs--still the top priority in Poland.

Ladies and Gentlemen, I am convinced that the opinions presented here on the subject matter of our meeting will be useful for all of us in the immense work for the economic development of our countries we, parliamentarians, still face today.

Nikolai Todorov
President of the Grand National Assembly
Republic of Bulgaria

Thank you Mr. Chairman. I would like to stress two things: That in our Parliament we are working hard in a very complicated situation without enough experience, with many suggestions from everybody. As you know, our assembly is

constituent. We were elected for the preparation of a new constitution. But, at the same time, one of the top priorities is to pass the fundamental laws for our country's transition to a new economy. A key place within that set of new laws is occupied by the privatization bill. Many members of our parliament see its passage in the parliament as the touchstone of a move from the centrally planned economy to a new market economy. At its call, we extend the algorithm of decomposition of the so-called state owned property and, in my opinion, into this algorithm we have to incorporate an algorithm of capital formation with two clear aspects: legal organizational aspects dealing with legal form of future autonomous economic entities and ownership thereof. And the second aspect, a proper assessment. The second algorithm is the question of capital balancing. And the third algorithm is capital functioning.

In this way you see the role of parliament is not very big; it is more or less restricted. But, legislative initiative should focus on the tools to be made available to the privatization party, to give that party shouldering the risk of capital balancing total capital management. We are sure that the question of the process of privatization must first be dealt with in our parliament. And to ensure comprehension, because only after that the executive branch of the government is given the go ahead.

In some small words I have tried to explain what we have to do. Because we must pass perhaps the more difficult law in our country--the law of dealing with privatization of land. You know that Bulgaria was 100% cooperative. The question is to put private ownership in a similar situation with the cooperative system. Maybe we shall have success but we have to see how we shall go further.

František Mikloško

Speaker, Slovak National Assembly
Czech and Slovak Federal Republic

The constant experimentation with trying to set up some kind of realistic socialism has devastated not only our political system and economy, but, even more serious, has had moral and intellectual consequences. So, these are the basic points of departure from which we are beginning to emerge and from which we are building bridges back to Europe. They are not good. We are returning to the only historically tried and true form for the dynamic development of a market economy society. What will be the tasks of Parliament in these new, to us, circumstances?

There is no doubt that the tasks of parliament in a democratic society and state under the rule of law for which we are striving, are of most extraordinary significance. We must guarantee our assumed intention/s/ in the transformation of our economy in the market mechanism and we must do this soon.

The greater complexity of the situation in which our Parliament finds itself is because the transition of our economy to a market mechanism is occurring under conditions under which we are also attempting to create new relationships between our republics and this of the Czech and Slovak, in the framework of the new distribution of powers in our Czechoslovakian Federation. It is a question, therefore, of complicated negotiations of the authority relationships and powers of the /political/ bodies of the Republic. This occasionally causes delays in the legislative process.

We are at present in the first year of bringing about our economic reforms in which we are concerned with making the transformation from direct guidance of the economy to principles of the functioning of pluralistic forms of property and establishing these forms on an equal basis in the economic processes. Previously we established the essential legislation preconditions to introduce this system of guiding the economy.

A broad and complex amendment of all essential legislative acts was carried out beginning with fundamental changes in our constitution and constitutional legislation up to the adoption of countless individual laws. We resolutely adopted laws in the legislative sector with which radical changes in the property relations of the economy were accomplished.

As early as last year we began to effect this process which we call the process of small-scale privatization. This process has as its goal: privatizing the commercial sector, up until now exclusively state-owned, services, and non-agricultural production, thus shattering the /state/ monopoly and guaranteeing an environment motivated by competition. The laws in question have been adopted and we are beginning to bring about the far-reaching process known as the large privatization.

Other laws will follow breaking the state monopoly, destatization, and expansion of the private sector; laws which we say are of a "restitutional nature." We are not only concerned here that the illegally expropriated property be given back into the hands of the original owner and compensation be made for wrongs committed in the past, but also with the formation of a middle class of entrepreneurs who have a legitimate place in a market economy.

At the same time, we are making efforts towards the small and large privatization by means of the above-mentioned laws, in order to animate the economy even if this entails use of foreign capital. We must point out, however, that this is only a part of the comprehensive complex of systematic measures we have adopted vis-à-vis other countries in the interests of our economy.

We amended laws with which we liberalized generally the regime to facilitate capital participation by foreign countries and we are loosening up in various ways economic relations between our businesses and other countries and are readying such measures even in the area of foreign exchange.

Understandably enough, these are only the absolutely essential measures. The incredible burden of legislative work has made it impossible for us to adopt further regulations, whose absence makes itself felt, and foreign entities interested in commerce and trade in our country are being visibly affected.

Systematic measures are also being worked out concerning price liberalization, and other legal regulations are being written aimed at returning land and forest property to private hands, or to the original owners.

In 1991, we went at the restrictive nature of our budget with counter-inflationary aims. We are bringing about fundamental changes in budgeting even at the community level in connection with the newly structured system of community administration, built on democratic principles of self-government.

At the same time, we are taking unavoidable legislative and systematic measures in the area of employment and welfare protection. Entering into the new relationships of the market economy will unavoidably cause some casualties. We expect, especially in the initial years, a general decline in living standards and increased unemployment, previously unknown in our system. The causes for this condition must be sought in the past, when socialism was being established, with its artificial incentives, "full employment," and the low productivity resulting from these.

Agreements with the unions have also been made and we took steps towards making a fundamental social network. Employment offices were set up and other measures planned in the area of unemployment and social ills.

I have been trying to show you briefly some of the problems we are having to deal with at present. I believe that in our efforts to solve these problems, we will also receive some effective aid from the developed part of Europe and, also at the parliamentary level, we will succeed together in finding solutions to a number of these problems.

Dan Martian
President, Chamber of Deputies
Romania

Mr. President, Ladies and Gentlemen:

I would like to thank the outstanding International Foundation for the Survival and the Development of Humanity, as well as our host, the Hungarian Parliament, for the invitation addressed to the Parliament of Romania, and for the hospitality we are all enjoying; I would also like to express my satisfaction and my colleagues' satisfaction at

having the privilege to take part in a conference with such a generous purpose. The themes of the conference are all the more topical for us who come from countries where, because of complex adverse conditions, we lived for over four decades under a totalitarian regime that impregnated almost all the pores of the society.

It is a bitter truth, that no one could deny today, that during the period of dictatorship one of the most severely affected sectors was the economy, subject to numerous conceptual, administrative and juridical traumas, dominated by a rigid, centralized and anachronistic mechanism in total contradiction with the requirements of the modern market economy. This detrimental situation had an impact over the entire economic, social and political life in our country.

In this general context, the revolutionary events of December 1989 that put an end to the totalitarian communist regime in Romania marked a turning point in the evolution of the entire Romanian society.

In the conditions of the establishment of a pluralist democratic political system and the separation of the powers in the state, major responsibilities are incumbent upon the Parliament of Romania. The Parliament resulted from the election of May 20, 1990, and is made up of the Deputies' Assembly and the Senate; as the unique law-making authority in the country, it is meant to translate into appropriate laws the firm option of the electorate in favor of our country's keeping abreast with the states having democratic traditions, and in favor of its compatibility with the developed economy. An eloquent proof of the intense legislative activity carried on in the nine months elapsed since the constitution of our parliament is the fact that during this period it adopted over 70 laws.

It goes without saying that among the legislative priorities and preoccupations of the Parliament, the economic reform holds the first place; the general conception of this reform was mapped out by the President of the country on the occasion of his investiture and then materialized in the governmental program approved by the Parliament. Thanks to its global character and its content, the economic reform embraces all the spheres of economic and social activity, marking an essential change of system.

The transition to the market economy, a process far more complex and profound than the placing of the economy under state control -- which was the result of an act of command based upon coercion, imposed over 40 years ago -- requires, in the first place, the setting up of a legislative framework capable of unblocking the various sectors of the economy, stimulating private initiative and changing the relations of ownership.

In this respect, the first step in the field of legal regulations was the series of laws concerning the institution of the economic factors specific to the market economy. It was thus that were adopted the Law on the reorganization of state-owned economic enterprises as self-managed enterprises and trade companies, the Law on the trade

companies and the Law on the trade register. In terms of these laws, the relations between the state as an owner and the economic enterprises change, as the state relinquishes its role of direct administrator of the enterprises, becoming their creditor.

We have decided to go ahead. The bill on privatization is being drafted now, its basic principle having been established by the Law on the reorganization of state-owned economic enterprises as self-managed enterprises and trade companies. In terms of this law, every newly-founded trade company will place 30 percent of its registered capital at the disposal of the National Agency for Privatization. The agency will issue registered bonds of 5,000 lei each, which will be distributed equally and free of charge to all the Romanian citizens resident in the country who reached the age of 18 by December 31, 1990.

An important legislative act recently adopted by the Parliament--the Law on the Land--does away with one of the most flagrant cases of injustice of the former communist regime, giving back the land to the peasants. The law stipulates the restoration of the right of ownership over the lands held before the collectivization of agriculture and the allotment of plots of land to several categories of agricultural workers, being likely to open up wide prospects of assertion to the economic and commercial relations based on private property, to bring about fundamental changes in the whole social life of the Romanian villages.

The draft law on the authorization of buildings and the promotion of the building of houses and holiday dwellings also aims at the development of private property, as it ensures the general framework for the development of private or public constructions.

Taking into account the significant role played by the financial and banking system and its levers in the market economy, the Parliament adopted a series of laws in these fields, too. Under the new conditions, the financial relations between the enterprises and the state are achieved through the system of taxes and dues regulated by the law on public finance and the law on the income tax. The law on the organization and functioning of financial control and the Financial Guard, and the Law on the individual income tax have also been adopted.

At present, we are debating legislation concerning the banking system which will consecrate the separation of the National Bank, fulfilling the role of central bank, from the commercial banks, whose role is to attract and turn capital to account.

In order to facilitate the constitution and the functioning of a true labor market, a series of laws have been promulgated with the aim of giving more freedom to the employees and the enterprises in establishing contract-regulated labor relations. The Law on the engagement of employees according to their competence is completed by the Law on the plurality of offices and the Law on salaries. The latter promotes the principle of free negotiation of salaries within each trade company, according to its

financial possibilities. The Law on the individual income tax is in the final stage of promulgation.

One of the basic ideas of the law-making activity in the field of economic reform is that it should be carried out so that the social security of all employees may be ensured. The intention is that the minimum salary at national scale should be approved by the Government, taking into account the dynamic character of the salary which depends on the evolution of prices and of labor productivity. The Law on the collective working contract stipulates the rights and mutual obligations of the employer and the employees with the aim of promoting working relations likely to ensure the social security of the employees. The Parliament has also debated and adopted laws on the unemployment benefits and the professional reintegration of the unemployed, and on the solving of collective working conflicts.

The draft law on social security is also being elaborated; its provisions concern the organization of the system of social security, the constitution of the social security fund and other measures meant to contribute to the significant improvement of social security of the population.

Another field of activity of the Parliament in promoting economic reform is the institution of basic rules for the carrying on of commercial relations within the market economy; these rules differ from those established by the Commercial Law and the Common Law and refer to the suppression of illicit speculation, unfair competition, tax evasion, contraband, etc.

One of the first steps taken in the economic field after the elimination of the state monopoly over foreign trade was the creation of conditions far more favorable to the activity of foreign capital. At present there are in Romania a large number of companies with mixed capital or foreign capital exclusively; the Parliament is debating a law on foreign investment. Romania's opening to Europe and the world economy has been supported by a series of laws such as those on the ratification of the Agreements between Romania, on the one hand, and the EEC and Euratom on the other, laws on trade and commercial and economic cooperation, on Romania's adherence to the United Nations Convention on contracts of international sales of goods, and other laws on the adherence to a series of international conventions and treaties.

There is no doubt that the development on the way of economic reform is all the more fruitful as it goes hand in hand with the strengthening of democracy and the state of law. As a consequence, the preoccupation of our Parliament to ensure the judicial framework necessary for the development of the market economy has been combined with the process of elaboration and adoption of regulations likely to contribute to the democratization of social life, a process materialized, for instance, in the set of laws concerning citizenship, the administrative dispute claims, adoption, etc.

As is known and, in a way, was expected, the problems of the continuous democratization of social life are particularly complex, for Romania, as well as for other countries that have recently freed themselves from the totalitarian communist rule and have embarked upon a road yet untrodden towards a new democracy. Of course, the development of the democratic structures will exert a beneficial role in the process of consolidating the market economy. It also goes without saying that the vast and complex problematics of democracy will acquire new dimensions once the new Constitution is adopted.

In this connection, we would like to remind that the Parliament of Romania is also fulfilling its function of Constituent Assembly and that, in this capacity, it is fully engaged in the process of debating and adopting the Theses for the elaboration of the Draft Constitution of Romania. The conclusion of this activity will certainly mark a major step towards the establishment of the fundamental judicial framework of the country and implicitly for the guarantee of the functioning of the state of law.

With the aim of democratizing state activity and consolidating the principle of separation of the powers, the Parliament of Romania has adopted several other laws on the organization and functioning of the Presidency offices, the organization and functioning of the Government and several ministries, of the local bodies of state administration, as well as on the strengthening of the authority and independence of the judiciary.

Mr. President, Ladies and gentlemen,

It goes without saying that this statement was not meant to give an exhaustive image of the responsibilities and role our Parliament is fulfilling in the process of Romania's transition to the market economy. We merely wanted to submit to your attention some of our legislative preoccupations and activities hoping that the exchange of experience and opinions in the framework of this conference will enable each of us to draw the conclusions we deem useful.

We believe that such international meetings that result in an increased number of exchanges of delegations, of regional parliamentary roundtables and conferences are likely to contribute to the diversification and strengthening of mutual cooperation, for the benefit of all.

Bogdana Glumac-Levakov
Speaker, Federal Chamber of the National Assembly
Socialist Federal Republic of Yugoslavia

Ladies and Gentlemen:

Allow me on behalf of the delegation of the Assembly of S.F.R.Y. to express our appreciation for the invitation to this international conference and for this opportunity to present a brief overview of the reform process that is currently underway in Yugoslavia and the role of Parliament as the supreme legislative body in that process.

According to the provisions of the Constitution of S.F.R.Y. as the supreme legal document, the Assembly of S.F.R.Y. is the highest organ of authority within the framework of the rights and duties of the federation and as the supreme legislator it exercises its rights and duties on the basis and within the framework of the Constitution and federal statutes.

Through the work of its Chambers, the Assembly of S.F.R.Y. formulates both current economic policies and development policy in various areas of the economy which are important for the functioning of the unified market and the federal administration.

The changes in our country are being implemented to the backdrop of turbulent and far-reaching developments throughout the world and particularly in our part of Europe. Yugoslavia cannot be immune to nor isolated from such developments.

Before focussing on the main theme of our deliberations allow me to recall that multiparty elections, the first since World War II, have been held in all the Yugoslav federal units. The federal agencies are now composed of representatives of various parties which means that diverse ideological and political orientations are in evidence.

The election of delegates for the Chamber of Republics and Provinces is nearing completion but secret, federal elections for the Federal Chamber have yet to be called.

We have clearly embarked upon a thorough reform of the system and there can be no going back without serious consequences. The departure from one system and the establishment of a new one requires a great deal of experience and expertise which is derived from our own experiences and knowledge but drawing fully on world-wide experiences regarding global development.

The extremely unfavorable economic and political conditions in Yugoslavia today make it increasingly difficult for the Assembly of S.F.R.Y. to carry out its tasks. The success of the work of the Yugoslav parliament can be said to hinge on the quality of the decisions it takes and there is no doubt that only a common, generally acceptable concept of the reform can ensure for Yugoslavia an early surmounting of the crisis.

Towards the end of 1989, the Assembly of Yugoslavia approved the economic reform program prepared and proposed by the federal government. The aim of the program was the full assertion of a market economy and ensuring the necessary preconditions for bringing Yugoslavia's then spiralling inflation down. This program identified three key goals of the reform:

First, the introduction of an integrated market in Yugoslavia which meant the further development of the market of goods and services and the affirmation of the market of capital and the market of labor.

Second, introducing national integration into the world economic system, and

Third, the strengthening of the rule of law and the expansion of human rights in accordance with international standards as well as the introduction of a pluralistic political democracy.

The market-oriented economic reform program focused primarily on the development and affirmation of markets of goods and services, labor and capital, and the strengthening of monetary and fiscal management. To that end a number of laws regulating these areas of the economy were adopted last year.

The premise underlying the reform of the economic system is the business autonomy of enterprises and banks based on the integral functioning of the markets of goods, capital and labor. In the area of property relations, the principal novelty is the introduction of a pluralism of ownership forms and their equal treatment. This means that all ownership forms, i.e. social, private, cooperative, mixed and wholly owned foreign enterprises enjoy equal status and can be easily transferred from one form of ownership to another. Joint stock and all other kinds of companies that exist in any free market economies can also be formed in Yugoslavia. The principal target of an enterprise is the maximization of profit. Banks are also being transformed into shareholder societies that are fully independent in their operations. Competition in the banking sector is being encouraged through the possibility of the formation of mixed banks with the foreign partner enjoying national treatment. The National Bank of Yugoslavia ensures unity of the monetary, foreign exchange and credit systems. It is autonomous in its money supply policy. A money market has been introduced and provisions adopted on the introduction of a capital market. Measures have been taken to tighten financial discipline of enterprises and banks. A significant degree of deregulation has been effected and the foreign trade and foreign exchange systems have been fully liberalized.

An entirely new and attractive regime of foreign investment in Yugoslavia has been put in place identical to those in market economy countries.

A common feature of all these reform undertakings is that they are geared to increasing efficiency of the economy and society as a whole. In order that this course

of development should be lasting, stable and effective, it is essential that the economic reform be attended by a reform of the political system, the continuation of the constitutional reform and the affirmation of the state of law. Together with the work on the finalization of the regulatory framework for the economic reform to be successful, those are at the same time the main thrusts of the current activities of the Yugoslav parliament.

Yuri V. Blokhin

Deputy Chairman, Supreme Soviet Committee on Economic Reform
Union of Soviet Socialist Republics

Mister Chairman, Ladies and Gentlemen:

In my brief address I would also like to talk about the work which is being conducted in the Soviet Parliament on developing market relations with the goal of creating a more efficient and dynamic economy which guarantees the citizens economic freedom, an economy which is socially oriented toward consumer demand, one which creates conditions for encouraging industry, creativity and initiative.

Despite differing opinions about ways of moving toward a market economy and even some opposition, at the present time Soviet laws are being adopted and are in effect on ownership, on the foundations of land legislation and land relations, on enterprises, on a unified taxation system, on mutual economic relations between the Union of Soviet Socialist Republics and federated subjects, and so forth.

The most concentrated study on ways of developing a new economic system is in the "Basic Guidelines for Stabilizing the National Economy and Transition to a Market Economy." They identify the logic and phases for healing the economy and shifting to a market economy; measures for stabilizing the economic situation in the country and formulating a market economy; and the issues of social, structural and investment policies during a transition to a market economy, and the reorganization of the system for managing the national economy.

Strictly speaking, all of the subsequent activity of Soviet members of Parliament is in total accord with the above-mentioned "Basic Guidelines."

Today, the nation's economy is in a severe state due to inconsistency and indecisiveness in the conduct of economic reform. A drop in production and a lower standard of living have resulted from the scrapping of old structures of the administrative command system of managing the economy and a lag in developing a new system of economic relations.

In this situation, we need more decisive preventive actions which are capable of stabilizing the situation in the economy and creating conditions for rescuing it from a crisis situation.

In this regard, the U.S.S.R. Parliament and Presidium have prepared and undertaken an entire series of legislative acts to normalize finances and monetary circulation, measures to stabilize the consumer market, conduct a pricing policy, and ensure the public's social security and the stability of economic relations.

At the same time, we are performing legislative work to support free enterprise, destatization, privatization and the development of competition.

A draft law entitled "On General Principles of Free Enterprise in the U.S.S.R." has already undergone a first reading. We determined the general principles of free enterprise in the U.S.S.R., the rights and obligations of the subjects of free enterprise activity, their state protection and support and interaction with the organs of state control. The law is geared toward creating conditions for citizens' broad manifestation of economic initiative and free enterprise on the basis of the realization of the principle of equality of all forms of ownership, including private ownership, and the freedom to dispose of property and choose a sphere of endeavor.

At the present time, another draft law entitled "On Denationalization and Privatization" is being prepared for examination in a first reading. By privatization we mean a non-obligatory transition to private ownership only, and the more general process of replacing the owner through a transfer or sale of state property to labor collectives, cooperatives, stockholders, foreign firms and private individuals on various conditions.

On the whole, while creating a lawful basis for regulating free enterprise and developing the processes for denationalization and privatization, we proceed from an understanding of our realities, which are collectivist and are based on the solidarity of the structures of our society, and the absence in our country of an entrepreneurial class with a specific motivation, culture or ethic. Here the experience of Japan is extremely useful to us. It is based not on the destruction of structures of traditional society, but their use. There the stage of industrial competition has not been skipped, and relations of solidarity, planned responsibility, non-market honor and ethics have not been destroyed. Cosmopolitanization and denationalization of the consciousness have not taken place.

With the foundation of a new economic system, we are linking the creation of a branch network of small enterprises. In our conditions, where over 30 percent of all enterprises are large monopoly enterprises, the creation of structures of small enterprises will enable us to soften the impact of privatization of state enterprises in connection with a sharp reduction of work places. It will serve as a sort of sponge which will suck up surplus manpower. In this regard, we must adopt a law on the

development and support of small enterprises (although a government resolution has already been in force since July of last year).

Among the laws which form the lawful environment of the market mechanism of self-regulation, I should also mention the laws already in force on the U.S.S.R. State Bank, on banks and banking activity, and on hard-currency regulation and investments.

In addition, during the course of the Soviet Parliament's current work, we must examine these draft laws: "On the Foundations of the Legislation of the U.S.S.R. and Republics on Price Setting," "On Anti-Monopoly Activity," "On Bonds and the Stock Market," "On Competition," "On Foreign Investments," etc.

By adopting all of these laws, we hope that we will create the necessary conditions for progress, although we realize that this is not the end, but only the beginning of even more work in our nation on economic reform.

In this regard, we are confident that today's shared experiences and ideas on the ways and mechanisms for activating economic development on the basis of market relations will undoubtedly be very useful for all members of Parliament who understand legislative activity in the economic sphere.

III. DEMOCRACY AND MARKETIZATION

Highlights and Commentary

The simultaneous development of a democratic political system and a market economy undoubtedly is more difficult than the achievement of either objective alone. Marketization imposes high costs on the population in the early stages, as production and living standards fall, unemployment and prices rise, and resources are redistributed according to market principles. At the same time, democratization provides opportunities for different groups to press their own demands and interests, potentially conflicting with the perceived interests of an effective national economic policy.

Despite the tension that may result from this process, all participants agreed that democratization and marketization are complementary and interdependent. Both processes are necessary for dismantling the old administrative-command system. In the economy, market signals of supply and demand must replace state orders; and in politics, diffusion of power and consensus-building must replace the self-empowered, centralized, command authority.

Differences were evident, however, on the question of how to build new political and economic institutions and on the extent to which old institutions may be relevant. Some countries (Hungary, especially) emphasized the possibilities for drawing on historical experience, reviving institutions that pre-dated the command system. Some from the U.S.S.R. expressed an interest in using existing institutions to build a new, democratic market system, citing the Japanese experience as an example of successful transformation with some degree of institutional continuity.

A new process of decision-making underlies both democratization and marketization, in which diverse interests compete and trade-offs among interests are decided through compromise. Such trade-offs are embodied in all the central tasks of economic transition: in developing a comprehensive economic program that balances the objectives of monetary stability, growth, and employment; in international integration that balances domestic and foreign interests; in privatization that is efficient and fair.

The parliament can serve as a vital forum for public discussion of the choices involved in marketization. Moreover, it may be a mechanism for balancing competing interests -- whether among groups in society or among regions -- in the formation of national policies. In fact, differences of view within the parliamentary delegations -- over the pace and content of reform -- were evident; many participants acknowledged these differences and urged cooperative work within the parliamentary process to advance the common core interests of their peoples.

Still, the tension that may arise between serving particular constituent demands and the "common good" of the nation creates dilemmas for legislators. In general, most

participants urged that parliaments rise above particular political interests and "emotional" arguments in order to resolve the fundamental issues of transformation. While relatively little concern was expressed about the possible adverse effects of populism, some participants noted the need to mobilize the population to support and assist economic transformation, while avoiding resort to irresponsible political tendencies. All the countries clearly are looking for ways to move forward on economic transformation while minimizing social costs, yet popular resistance to the required sacrifices remains a serious problem.

Moreover, democratization and marketization have meant a redefinition of relations between local/regional governments and the central government. The problem of decentralization of economic and political power was noted by several participants as a complicating factor in economic transformation. A representative of the Czech and Slovak Federal Republic emphasized that legal, parliamentary procedures, though slow and cumbersome, are the only legitimate way to resolve disputes between regional and central authorities.

Even if these fundamental issues can be overcome and consensus reached on particular trade-offs, a variety of other constraints on the parliaments were described which may inhibit movement toward economic transformation. One problem concerns implementation of laws; it was argued by some that the parliament needs greater oversight and enforcement powers to ensure effective implementation. A second constraint in some countries is the composition of the current parliament. Those not elected in direct, popular elections may be perceived as lacking legitimacy with society and therefore, their acts may be met with greater resistance (Poland). Moreover, the indirectly elected parliaments may contain elements reluctant to pursue transformation, making decisive action toward marketization much more difficult (U.S.S.R.). Finally, the limited expertise, research facilities and staff support available to the new parliaments further constrain their ability to formulate effective programs.

In resolving these tasks, each country and each parliament will determine its own balance and solutions. But, by seeking to develop a social consensus behind reform programs, the democratization process itself will strengthen the sustainability of market reform. If, on the other hand, marketization is pursued without public support, both marketization and democratization may be jeopardized.

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József Antall
Prime Minister
Republic of Hungary

Ladies and Gentlemen,

In the name of the Hungarian Government I would like to welcome you. I am pleased to see this exchange of views addressing the basic problems of our region take place in Budapest, in our Parliament. In my opinion, the role of parliaments is essential, as they represent the basic difference that sets dictatorship apart from democracy. This is why I am especially happy to welcome you here and, at the same time, I would like to thank all those who made this conference possible.

A lot can be said about the role of a parliamentary government in a transitional period, but I don't want to bore you with this subject. The most important question at this time of transition is the possibilities and limits of government intervention in a parliamentary democracy. In Hungary this question is more than 100 years old. It was debated as early as the mid-19th century when socialism and market economy were only theoretical issues. The basic question was posed by József Eötvös in 1865 as follows: Is it ownership or the power of government that provides stronger motivation to work? At the time it was a theoretical question. Today I am convinced that the unequivocal answer to the question posed by Eötvös is: Ownership provides a stronger motivation to work than the power of government. He continued his reasoning by stating that in comparing two political systems, the basic distinguishing factor is: which one can provide more for its people in terms of material well-being and intellectual values. Is it the (then) existing, i.e., bourgeois, system or the new socialistic theories? This question has been answered, too, even though, from an historic perspective, no one can question the positive role of the socialist ideas or even the different trends of the labor movement in our endeavors to create a welfare state. The real question is how these economic and political differences manifest themselves in a period where we are attempting to make the transition from a centrally planned economy to a market economy.

During the past decades, the market economy existed side-by-side with the planned economy as a reform experiment. The idea of implementing the laws of a market economy to a limited extent has often come up during these past few years. Even before, but especially after, 1956 such efforts took place under different names and circumstances permitted by the political limitations and opportunities. In 1956, under different historical circumstances, both communist and non-communist political forces entertained the illusion that socialism could be reformed and democratic socialism in a political sense had a corresponding economic formation that was compatible with market economy.

In the early 70s and 80s it became clear and widely accepted that a market economy is not compatible with political dictatorship. Therefore, any theory separating political from economic democracy was doomed from the beginning. Political efforts that were based on an attempt to meet the requirements of a market economy, but neglected to establish a democratic system of political institutions, in other words, intended to create a market economy within a one-party system, were dead-end propositions in the past decades and the past years.

In different countries of the region there have also been different political trends and efforts; but in Hungary all the political parties represented in the Parliament--not only the five political parties that used to be in opposition, but even the successor of the former state party--have come to the conclusion that market economy and dictatorship were not compatible. In 1988-89 it became clear that Hungary would take the road of a multi-party system and nothing could prevent the creation of a multi-party political democracy. Since the beginning of 1988, all significant political forces have included the cause of political democracy, multi-party system and market economy in their platform. We feel that in this area Hungary has no cause to be ashamed. The transitional character of the period was apparent in the legislative activities of the latest session of Parliament and in the activities of the government of the transitional period. As of 1989, the changeover and corporate law were clear steps in the direction of market economy and a system of supporting institutions. In 1990, following the elections, the new Hungarian government was formed with a 60% majority, according to the proportion of forces in the Parliament. It established the conditions for parliamentary activities and parliamentary government in the Hungarian political system of institutions, despite all the difficulties and problems. We must applaud the fact that a government coalition with an absolute majority was formed, along with a strong and significant political opposition, creating an authentic political democracy and parliamentary system in Hungary. It is a politically outstanding accomplishment that, in spite of all the difficulties, a stable government and--I am happy to report--a stable opposition are fighting out their political battles within the Parliament.

The other achievement is that, with the Parliament, the Government, the Constitutional Court or with self-government established, not only the system of institutions of political democracy were created in 1990, but also the system of institutions of economic democracy is being developed, with many important institutions already in operation.

In spite of the difficulties experienced by the Hungarian banking system and the limited capital available, the Hungarian Stock Exchange was established; it can be regarded as the basis for a banking system rooted in a market economy. Furthermore, in addition to the above-mentioned political laws enacted to develop the administrative institutions, several bills and amendments that can and do play an important role in building a market economy have been enacted during the existence of the new Parliament. These include: the pre-privatization law; the indemnification bill for settling proprietorship disputes, now under debate; the concession bill, which is under

discussion by the plenum, and which is to regulate the questions related to ecclesiastical and self-government ownership; in other words, all the bills which have been prepared and which form the legal framework for a market economy as part of a general strategy for establishing an economic policy.

These are the circumstances under which the government must deal with the problems characteristic of the whole region, resulting from several decades--four in Hungary--of dictatorship and a centrally planned economy.

These problems arise not only from the established system of institutions, the heavy debts and the fact that these countries have been part of a huge but limited internal, colonial type market, but from the fact that during these decades people's attitude towards ownership has changed; they remained unaware of the institutions and structures that drive today's modern market economies. In addition to the heavy debts and structural difficulties, the greatest problems this region has to face are in the field of human attitudes towards economic management and economics. Governments accountable to their parliaments have to do their work overseeing the transformation under such circumstances. This means that our possibilities are limited, both the public and foreign investors expect faster action and more effective measures to change the economy.

We cannot ignore the fact that we must carry out our administrative and legislative work at a time when quick and effective measures are needed. However, right from the beginning, we chose a strictly constitutional, parliamentary method of accomplishing these tasks, and governing in a parliamentary system is very time-consuming. But we are convinced--this is not the first time I am saying this, neither am I the first one to say so--that nothing better than the parliamentary system and parliamentary democracy has ever been invented.

Our government, facing the day-to-day problem of how to carry out this transformation in the fastest and most effective manner, must operate within the existing constitutional state and its laws. This is our objective.

I don't want to take up any more of your time. On behalf not only of Hungary but of all the former socialist countries in this region, I would like to call your attention to the fact that revitalizing the economies of this region is in the interest of the entire developed world. Failure to accomplish this may result in social tensions, political instabilities and even major shake-ups in Central and Eastern Europe, endangering democracy and a market economy, especially in view of other tensions that are characteristic of this region. It is very important to establish the conditions for a well-functioning democracy in our region within the political and economic system of institutions, the system of interests, and a partnership between employers' and employees' organizations capable of channeling the interests and emotions of both parties. We need the participation of all for democracy to succeed in our area. In my

opinion, the conditions are there; we need patience, support and consideration for the human element.

Francis Miko

Specialist, Soviet, Central and East European Affairs
Congressional Research Service

Three elements of the current process of transformation of the Central and East European countries deserve particular emphasis: First, the linkage between democracy and successful market reform is complicated and in some countries unresolved. Second, parliaments play the critical role as the institution bringing the two processes together and managing the simultaneous development of both. Third, regional cooperation and sharing of experiences among governments and parliaments can contribute to strengthening democracy and market reform in each of the countries but are probably not utilized enough. The Budapest Conference on the Parliament's Responsibility for Economic Development addressed and -- by the fact that it was held in the Hungarian Parliament with participation of newly elected leaders from all of the East European parliaments, the Soviet Union, as well as the United States and Germany -- underlined these factors.

Linkages between Democracy and Market Economies

Two of the critical questions now facing Eastern Europe are: (1) Can democratization and market reforms be pursued simultaneously by former Communist countries? And, if so, (2) must they be pursued simultaneously to ensure a successful transformation?

Many of the countries of Central and Eastern Europe are already trying to answer in the affirmative by making democracy and free-market economies central principles of their new systems, as fundamental ends in themselves. In other countries the necessary linkage of the two processes is still a matter of debate. In some quarters, fascination is still discernible with authoritarian models of market reform. The examples of Pinochet's Chile, South Korea, Taiwan, and other countries are sometimes cited.

Even those formerly Communist societies which have made the commitment face issues and tensions in trying to pursue both democratization and marketization. The conventional wisdom is that political change was relatively easy; economic transition will be a much more difficult and lengthy process. While this may seem true on the surface, political and economic change remain linked, since many of the key difficulties and barriers to economic change are political. Also, failure to achieve successful economic reform could undermine the fragile democracy that has been achieved.

The central dilemma for all of the emerging democracies is that while over the long term, democracy and market systems hold out the promise of raising living standards and providing greater freedom, over the short term the transformation is causing a great deal of suffering.¹

No one knows exactly how high the costs or for how long, since no country has yet completed the transition from a Marxist-Leninist system to a free-market one. This raises a fundamental question: Can the short-term sacrifices needed for market transformation get public support in a free and open system? And if so, for how long? Opponents of immediate adoption of Western style democracy argue that the two cannot be pursued simultaneously given the bitter pill of adjustment that has to be swallowed by society. The question seems particularly relevant since, in most East European countries, both the democratic systems and the governing coalitions are still weak. Also, as a result of the legacy of the past, the distrust of governments and parliaments by the population remains, even after free elections.

Some recent findings, though, suggest that the democratic base in Eastern Europe may not be as fragile as feared. According to one of the largest three-country public opinion surveys ever done in the region, sponsored by Freedom House and the American Jewish Committee, very large majorities in Poland, Czechoslovakia, and Hungary support democracy, privatization and a free market system, even after a year of considerable deterioration in their own living standards.² This is true despite the fact that a large majority expect economic conditions in their country to get worse in the next few years. In all three countries, short-term pessimism is balanced by a much greater sense of optimism about the long-term prospects for themselves and their country.

The negative features and problems of pursuing radical economic change under democratic conditions are well known. Democracy and economic reform can be mutually inhibiting in a number of ways:

-- Now that the very broadly shared goal of defeating Communism has been achieved in a number of countries, the strong political consensus is eroding on specific issues, though not on the basic questions of political and economic orientation. In other countries, broad consensus has yet to be achieved, even on basic economic or political goals.

¹ This summary overview draws on the framing paper for the Seminar in Budapest, March 1991, "Parliament's Responsibility for Economic Development", by John P. Hardt and Jean F. Boone.

² Democracy, Economic Reform, Western Assistance in Czechoslovakia, Hungary & Poland: A Comparative Public Opinion Survey. A poll conducted for Freedom House and the American Jewish Committee by Penn and Schoen Associates ... April 1991.

-- Democracy allows the free expression of rising expectations and impatience for results. These are likely to be in conflict with the economic requirements for belt tightening, austerity, and deferred benefits to populations whose expectations have already had to be deferred for years.

-- Democracy can magnify and give political clout to competing special interests, often contrary to national economic policy and the requirements of a quick transition to the market.

-- Democracy brings to the fore popular demands for justice and redressing of wrongs committed under the previous system. Yet, requirements for righting earlier wrongs may not always coincide with the interests of efficient and effective economic transition. This is especially evident in the areas of privatization and restoration of private property.

-- As a result of the above factors and inherent inefficiencies, the democratic process slows the implementation of market reforms at a time when most economic experts argue that a quick and deep transition to the market is needed.

These negative features of attempting simultaneous democratization and creation of a market economy must be balanced against positive ones. Successful democracies and market economies have a number of similar requirements and as they are fulfilled, the democratization and economic reform processes may prove mutually reinforcing.

-- Both democracy and a market economy require the emergence of a strong civil society, which has been defined as a society that is "autonomous and self-limiting." A civil society, in turn, is likely to demand both. Both also require the existence of a strong entrepreneurial middle class.³

-- Compromise is a key element of both democratic and market systems. In fact market economies based on coercion and command are seen by many experts to be a contradiction.

-- Democratic systems and market economies both demand social mobility, elimination of class barriers, and opportunity for all. If every major segment of society is to support the new systems, then all must feel confident that they can share in the fruits of the transformation.⁴

³Shopflin, George. Eastern Europe: The Outlook for Democracy. Radio Free Europe/Radio Liberty Research Institute. Soviet/East European Report, Vol. 8, no. 23, March 10, 1991. p. 2.

⁴Shopflin, p. 2.

-- Although democracy makes decision-making on highly controversial issues much more difficult, the decisions reached in a free and open process are likely to have far greater force, than those reached by government fiat. In the very difficult transition period, only the economic policy decisions made by freely elected governments, with the approval of parliament, will have legitimacy.

Central and Eastern Europe also face strong external incentives for treating democratization and market reform as inseparable. These coincide with Western conditionality in two areas:

-- Commitment to democracy and a market economy are basic conditions for Western bilateral and multilateral assistance, which can play a crucial role in the successful development of the region, in the short term. The United States has spelled out these conditions very explicitly, under its policy of differentiation.⁵ Other countries and international organizations also set conditions, either explicitly or implicitly.

-- Over the longer term, establishment of a stable democracy and market economy are likely to be a minimum price for integration with Western Europe. Most Central and East European countries have declared eventual membership in the European Community as a priority goal. Until full membership is possible, most governments are seeking the closest possible association agreements with the EC. Some of the East European countries are already fashioning laws and regulatory structures to be consistent with EC norms. Such norms are also likely to be the standard for fundamental East European legislation affecting democracy and economic policy. Other regional groupings of East and West European countries are possible, through the European Free Trade Association (EFTA) or new structures. In no case are West European countries likely to agree to close associations with East European neighbors that are not based on similar values and functioning democratic and market systems.

In the end, many experts believe that the countries of Central and Eastern Europe, even the Soviet Union, may have no alternative but to pursue both democracy and a market economy simultaneously, despite the difficulties. This course may be dictated by governments' requirement for legitimacy and the need to overcome entrenched groups that have strong vested interests in resisting change.

Role of Parliaments

As post-Communist governments pursue democratic transformation to market economies, freely elected parliaments occupy the central role. They provide the democratic arena in which the battle over economic policy is publicly fought. Their most direct function is to enact legislation, hammering out the necessary compromises between governing and opposition parties, representing the varying interests of the

⁵See U.S. Department of State. Focus on Eastern Europe, No. 26, October 19, 1990. 6 p.

electorate. Most parliaments have ongoing roles in implementation of policy through their committee oversight functions.

The parliaments also carry out other functions that are equally important to the democratic process of economic reform. The legislatures are the most direct representatives of popular will in the political process at the national level. In their deliberations, they provide the opportunity for all significant policy perspectives to be aired. In this way, parliaments provide an important educational role, helping to shape national consensus in areas such as economic policy. Most importantly, approval by the legislatures legitimates national policy in the eyes of the public.

In order for democracy and a market economy to develop simultaneously under current conditions, parliaments need to play a forceful independent role. If parliaments are seen as keeping a check on government policy, they can help to allay public uneasiness and disgruntlement over the government's programs. They can help to bolster public patience and tolerance, despite the expectation of continued decline in living standards in several countries in the near term, by fully airing the need for painful measures and the consequences of not taking them. Through this process, parliaments can also help to break down the inherited public suspicion of all government, its actions and motives. To more effectively play this role, all of the Central and East European parliaments must overcome their continuing negative public image. This image stems in part from an inadequate public understanding of the inherent messiness and inefficiency of parliamentary democracy and in part from the inevitable weaknesses of new and inexperienced legislatures.

Role of Regional Cooperation

Two types of regional cooperation could be very timely for the countries of Eastern Europe. The first involves mutual support in negotiating the transition. The second involves greater economic cooperation in the transition. It makes sense for post-Communist governments and parliaments to seek support, advice, technical assistance, and sharing of experiences, not only from the West but also from each other. As the Central and East European countries move to democracy and a market economy, they emerge from a common legacy of the previous system, are confronted by many of the same challenges and problems, and for the most part, are striving toward the same goals.

Central and East European countries have had to contend with the collapse of their previous Socialist markets, without yet being able to substitute Western markets for much of their production. Expanded economic relations, set up on a new mutually beneficial basis could provide a bridge, at least until they achieve competitiveness on the world market. Regional economic cooperation could be mutually attractive over the

long term as well.⁶ Given East European sensitivities, such relations would not have to be based on a formal new East European economic organization.

Yet, relatively little of this type of regional cooperation has taken place. The question is why? Several reasons can be identified. First of all, the East European parliaments have been too busy to reach out. They face enormous legislative work-loads with little experience and few staff. Second, there has been a tendency to see themselves as being in competition with one another in the race to join the West.

Perhaps the most important explanation is that each country has been soured by the legacy of "socialist integration", imposed from above. This type of regional cooperation, aside from not being one of choice, also did not serve national interests of individual members in many instances. A central part of transformation has been shedding the structures of regional integration such as the CMEA and Warsaw Pact. Now there is a strong reluctance to rebuild new regional structures with the same partners. Any economic organization of East European countries with the Soviet Union, unless it also includes major Western countries, is seen as a vehicle again exposing smaller partners to possible Soviet domination and retarding integration with the West. An East European organization without the Soviet Union also lacks wide-spread appeal. Such an organization has been labeled a "poor man's EC", and is also viewed as delaying union with Western Europe.⁷ The priority most Central and East European countries attach to union with the West has a strong economic rationale, but goes well beyond economic expediency to strong historical and cultural roots.

Yet there is much room for mutually beneficial regional cooperation, technical, political, and economic. Rather than compromising the newly restored sovereignty of individual countries, as many fear, such cooperation and coordination could strengthen independence by enhancing regional stability and reducing the potential for any power to play on suspicions and play off one country against the other. Western countries and parliaments may be able to facilitate cooperation and dialogue, through their own initiatives and active third party involvement.

⁶See Hardt, John P. *European Regional Market: A Forgotten Key to Success of European Economies in Transition*. January 25, 1991. 6 p. (CRS Report no. 91-113)

⁷This view was expressed independently by several members of East European parliaments.

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Many of the problems of the transition from centrally planned to market economies arise from the systemic interconnections of components of the socio-technological system that must be thoroughly restructured. In the view of the system that I propose, one can find five sub-systems. One of them, the institutional transactions system, is the one most closely connected with the work of parliaments. The problem is that it requires serious adjustment before parliaments in Central and Eastern Europe can begin to work effectively. At the same time, it is only one of five sub-systems all of which require adjustments and removal of disequilibria simultaneously. I wish to explain the special configurations of this system, both before and after the restructuring process is initiated that inevitably makes the restructuring in all of its dimensions very difficult.

The five sub-systems in the "model" are:

- 1) The technological-production system: the physical structure of factories and mines, their technologies, the transportation and communications facilities;
- 2) The commodity transactions system: the organization of production and distribution processes (the combinations of hierarchy, communes, and markets used);
- 3) The money circulation system: the organization of the supply of money and credit and of the demand for money either as a store of value or a medium of exchange;
- 4) The institutional transactions system: the political and legal systems that define the rules of organized social behavior;
- 5) The norming system: the organization of human interactions that generates norms of behavior.

The Difficulties of Restructuring

The difficulty of the restructuring process arises from several conditions, one of which is exogenous. The generally unfavorable international economy (slowing growth in the West, effects of the Gulf Crisis) have made it more difficult to obtain credits, find export markets and increased sharply the costs of crude oil. A related phenomenon is the breakup of the former CMEA, including the privileged purchase of Soviet oil and (implicitly) subsidized prices.

In addition, there are two endogenous conditions. First, all four systems not only are made up of components that are highly intra-system interdependent (i.e., within each

system), but also there are significant inter-system dependencies. What this means is that the effects of change in any one system or its component will be highly dependent on conditions in the other systems. For example, the capacity to undertake a correct sequence of changes in the system of commodity exchange will probably depend on whether or not appropriate changes can be initiated in the norming and institutional transactions system.

Second, at the time of the initiation of restructuring of the former system developed under communist rule, very significant suppressed disequilibria were found in all four systems. In fact, the state of economic, political and moral life was far more in a state of decay than most experts had imagined. Examples of the disequilibria are, in each case:

- 1) Damage to the environment at a rate that could not be sustained for a long period; neglect of infrastructure capital that could not be sustained in the long run; the increasing technological gap compared to the West;
- 2) Declining growth rates; increasing costs, including inventories, of production; increasing bottlenecks in the supply system; growing relative size of the second economy;
- 3) Increasing "monetary overhang" in the cash system and increasing resort to bank credit to finance both the state budget and state enterprises, with increasing unintended spillover of the cash system into transactions in the state budget and inter-enterprise transactions;
- 4) Increasing discordances between the constitutions and the administrative order, between the officially sanctioned institutions of parliament and the actual rule making organizations, and the increasing failures of political organization to give outlet to the diversity of interest groups;
- 5) Increasing gaps between the officially sanctioned norms and the actually practiced norms and the officially sanctioned institutions and the actually used ones, increasing disparities in perceptions and values among individuals, increasing inconsistencies in the values of one individual, as well as in connections of such values and realities--more examples of which will be discussed below.

The element of suppression was imposed by the system of political dictatorship and its ability to distort information about actual conditions and to provide both negative sanctions and upward mobility for favored cadres. In this way the command economy, for example, continued to be "workable", even though its weakness and relative ineffectiveness grew every year.

The major problem of the restructuring process is that as soon as elements of "openness" and "democracy" are introduced from the top down, be this in the form of

a deliberate Gorbachevian process or an unintended collapse in the rule of the communist party, all the disequilibria suddenly, so to speak, fly into the open. The formal system of order tends to collapse very rapidly.

As the collapse starts to take place, the main problem is how fast can the existing disequilibria among systems and their components be removed. The available evidence suggests that the time required differs very much across systems. At the same time, since the effect of any change is highly conditioned upon the status of the other systems, any immediately available change is likely to have the effect of exacerbating the collapse of both economic and political conditions in the country.

The Parliament's Special Problems

Missing constitutions, rules of parliament, and real political parties. The parliament's special problems arise in the first instance because fundamental constitutional issues are undecided. Nearly all of the newly elected parliaments in Central and Eastern Europe have the task of writing new constitutions. Beyond this, they lack efficient organization of their work; no one is setting daily agendas and effective organization of committees is lacking. Usually there is not available resources to help members of parliament maintain connections with those who elected them. That problem is made all the worse by the poor definition of political organizations. Political organizations, such as Solidarity and Civic Forum, that constituted the initial, anti-communist majorities, no longer reflect the diversity of interests in the new democratic societies.

Value chaos and misperceptions of problems. It is possible that the people of Central and Eastern Europe have even more diverse and potentially conflicting interests than do voters in the West. After all, they have been kept in "a value deep-freezer" by the communists. They have neither been exposed to issues like the civil rights or anti-war movements nor have they had a chance to build social-binding institutions such as churches and consumer-interest organizations. Finally, there is the problem that popular perceptions wrongly attribute such problems as open unemployment, open inflation, and even open knowledge of environmental problems to policies of post-communist restructuring rather than to the disequilibria inherited from the communist period.

IV. ECONOMIC PROGRAMS FOR TRANSITION TO A MARKET ECONOMY

Highlights and Commentary

The dilemma of choosing among or reconciling the goals of monetary stabilization, employment, and growth faces all of the transforming countries. These three objectives are key elements of the economic reform programs which these governments propose to their parliaments, their populations, and to international institutions; how they are met and balanced can be a crucial determinant of both internal and external support. In prioritizing legislative goals and setting their legislative agendas, the Central and Eastern European parliaments will influence the sequence in which these reform components are implemented and the extent to which they are interrelated.

The transforming countries are in different stages in the preparation and implementation of economic programs. While some countries are only beginning to debate the fundamental legislation for privatization, price liberalization, and foreign investment, others are already experiencing the tensions of implementation.

All seemed to accept in principle that economic programs, to be effective, should be comprehensive and simultaneous (that is, including provisions for price stability, growth, employment, and a social safety net), rather than focused on a single objective, such as monetary stabilization. Most acknowledged that "shock therapy" is not the only effective strategy for achieving monetary stabilization; some countries consider an approach in which reforms follow social preparation to be more appropriate and sustainable. Nevertheless, there are dangers with this solution as well, especially if the parliament is strongly influenced by social interest groups reluctant to make short-term sacrifices.

Economic growth and high employment are generally accepted as goals to be achieved along with price stability. For the transforming countries, one challenge lies in creating market incentives that stimulate productivity and growth. Restructuring the economy to enhance competitiveness and productivity may, however, carry high costs for some social groups in terms of employment and security.

There was considerable concern expressed about the need for a social safety net, but few concrete solutions found that could cushion social costs without counteracting economic incentives. It appears that unemployment is still low, even in the countries that have gone furthest in transformation, suggesting that old mechanisms of cushioning may still be operating -- that is, government subsidies and soft budget constraints on enterprises. Indeed, as Anders Åslund noted, the high rates of inflation that continue to plague Poland, Hungary, and the Czech and Slovak Federal Republic, despite restrictive fiscal policies at the macro-level, provide evidence of a lack of discipline at the enterprise level.

Moreover, the participants expressed clearly different conceptions of the state's new economic role. Though all the delegations espoused support for privatization, there were divergent views of the state's role in managing the process. Most delegations clearly favored market mechanisms as the primary instruments for state regulation, eliminating entirely the old administrative structures. Some in the Soviet delegation, however, indicated an interest in granting the state, and traditional institutions, a continuing role in guiding the economy. Also, where there was general agreement about the need for some government-administered social safety net, there was no agreement on how extensive it should be, or when it should be introduced, relative to other reform measures. Few addressed the specific problems of housing, medical care, and infrastructure (including the regional context) as priorities for government action.

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Tamás Szabó

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Political State Secretary, Ministry for Finance
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Esteemed ladies and gentlemen, allow me to express our heartfelt thanks and gratitude for the extremely interesting speech delivered by the Prime Minister of the Hungarian Republic, Mr. József Antall. On the basis of his contribution, we will be able to have a better understanding of the ideas which have a fundamental influence on the activities of the Hungarian government--their efforts in the period of transition toward a market economy, their efforts at strengthening the multi-party system in the country, and in ensuring the basic conditions for a democratic way of life in Hungary. As you all know, based on our previously set agenda, we will now switch over, we will start a roundtable discussion concerning issues directly related to the problems of the transition to the market economy and we will discuss also questions concerning cooperation in this respect among the parliaments of various nations. You are familiar with the topic, and if you agree with me, then we can now start discussing those issues.

Ladies and gentlemen, it is the second time that I have the microphone, although I haven't said much. Perhaps it will be boring to you, because what I am about to tell you is very closely related to what we have heard today. I start by saying that the market orientation of the Hungarian economy did have certain historical roots which did not begin with the new government. There was within the Hungarian economy for decades the logistics of the private economy--perhaps in the second or black economy, or perhaps in no more than the establishment of a private life sphere. But nevertheless, the Hungarian economy did possess knowledge and skill by the early 1980s which still retained something from the logistics of the old private economic

ways. The second thing is that, even during the reign of the previous government, they started to elaborate institutions which represented a movement towards a market economy. There was a taxation system introduced, the previous government introduced the Companies Act and the Investment Act which opened a gate for the further development of the economy. [Some] institutions [existed] in the days of the old government, as the prime minister has said--the stock exchange was already being established and furthermore, the state property agency was also established. I feel it is necessary to tell you that, because the possibilities for speeding up the development of the economy were created by those institutions and systems. In other words, we had something to build upon.

On the other hand, of course, we are fully aware of the heavy heritage of Hungarian history. We had a market which had no inner logic and which was totally isolated. As a result, we had to put up with a monocultural-like production system. We had to put up with the infrastructural delay or backwardness that we all know. As was said in the morning, this is one of the most serious issues. Then, the roaming inflation which started spiraling in the '80s. The Hungarian economy already carries the marks of a market economy but still suffers from something inherited.

The government was able to draft a program under the very hard given circumstances, about which I would like to tell you. We want to join in European integration. Several factors are already there for the transition. We have a well-established political situation for parliamentary democracy and we do have a relatively stable country in the political sense. Then we have privatization which is one of the crucial elements of the transition. We have several methods of privatization. During last year, serious steps could be taken both as far as the internal economy is concerned and on the international level--just to mention nothing else but the international balance. It is also a fact that Hungarian private enterprise started to boom during last year. Those are the processes which the program wishes to speed up. The objective of this package of measures is to stabilize the economy in Hungary and through that stabilization, to launch the Hungarian economy towards growth. This will also serve as a kind of indicator that will show us exactly where we are.

Convertibility contains the most important issues. The most important element is to develop private property. That is why one of the major directions is privatization. The second is to establish the legal framework for a market economy because the framework that we have, that would serve the market economy based on competition, cannot serve fully that economy. The third greatest danger is inflation--we must make efforts to fight against inflation. The fourth element is debt management. And number five is to limit the excessive state intervention, adopting behavior which would restrict the government's participation. Sixth, a social network that would provide some kind of help, assistance in the sacrifices made during the changes. And apart from creating a convertibility, we would like to establish an export-oriented economy which could truly solve the problems.

Allow me to give you a brief description of the most important details. Apart from the conditions already mentioned, we need to take the following steps. Within the Hungarian economy it will become obvious what will remain the property of the state and what will not. Privatization technologies will enter into force which, in the case of industrial branches, will make it possible for the nongovernmental sector, for market-oriented systems, because our experience shows that centrally planned and directed privatization has only limited effects. New institutions will emerge; those institutions are to be like the ones existing in Western Europe. We will summarize the experiences of our privatization process in a Privatization Act and it will be linked to a series of steps concerning de-monopolization. We will de-monopolize one company or one special field in the industry. Therefore the number of participants in privatization will increase.

The second topic I would like to mention is that we have to solve this year a new accounting act, a new statistical act and a new act on customs and duties. The bankruptcy law has also yet to be created. This will be the answer to the very tense question of the money market. There will be a financial law and there will be a law on concessions. Those are the most important. The deregulation process continues simultaneously with liberalization. In both fields the progress is very significant already.

I would only like to mention two sentences related to the program of anti-inflation. Inflation in Hungary is quite special because it is not that inflation is due to shortage or due to an excess demand; it is an inflation resulting from shocks and resulting from expectations. And the shocks are the result of a single change in many cases. It is a realistic assumption that inflation resulting from these kinds of shocks can be handled properly. I believe that our program includes those steps which can be efficiently implemented in order to limit inflation.

Now, may I proceed to the forthcoming topic. That is loans. In interest rate, the Hungarian economy has to pay \$1.5 billion in the form of debt service. At the same time, this is clear for us and the Hungarian government represents a uniform position when saying that this cannot require solutions which would give rise to an approach according to which the Hungarian capability to pay the debts would be challenged. We would like to solve all the problems in this area by attracting foreign capital, by increasing efficiency domestically. I believe that, in this respect, we can report good results in 1990 because we have an export growth amounting to 20%. Thereby a situation was created in which the performance, the output of the economy, was sufficient at least to cover our debt service. We also prepared an actual schedule for a period of three or four years [reducing the debt service] from 64 to 55-57%.

We would like to reduce the role played by the state in the economy. That is referring probably to subsidies. As far as the protective social net or network is concerned, we would like to set up a system of social institutions which would be capable to handle the unemployment which will be emerging as a result of the

transition taking place in the Hungarian economy. Besides this, the problem of poverty will have to be solved by implementing a poverty program. We would also like to concentrate attention at the various regions hit by crisis in our country.

If we had to sum up the major trends, tendencies, and processes, we foresee to take place in the forthcoming three or four years in the Hungarian economy, I would have to say that 1991 will be characterized by the re-arrangement, readjustment of the market, and the re-arrangement and restructuring of ownership. After 1991, we will have a realistic possibility to see a tendency for stabilization and anti-inflation so that symptoms of these two trends should be perceivable. If this comes true, 1993 could be the year of start-up and, parallel with this, it could be a year when our currency will be made convertible. Then in the forthcoming year after this, we could expect to see a certain amount of growth in our economy. It is important that the bodies for the representation of interests should be involved in these processes. Governing these tendencies in the true sense of the word requires quiet cooperation on the part of all the parties. Although we have been striving to achieve this, we feel we have a lot to do and I think it is a continuous process.

Anders Åslund

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The first year of transition to market economy in East-Central Europe has proved very difficult indeed. Much has been accomplished. A lot of new legislation has been adopted with the help of existing legislation in other countries. Domestic and external liberalization have occurred with surprising ease in Poland and Hungary. However, in order to assess the situation and prescribe policies for the future, we shall try to pinpoint what the main problem is. If, on the contrary, we were to focus on less important issues, there is a great danger that policies are put forward that are likely to aggravate an already difficult situation.

At the end of this paper, a summary of preliminary statistics has been listed. Most of these statistics are highly dubious, but even so a number of points are obvious. First, the whole of East-Central Europe is going through a very severe recession. In the region as a whole, national income fell in real (not official) terms by the order of 9 percent in 1990, with three countries (Poland, Romania, and Bulgaria) recording an official decline of more than 10 percent. The recession will be given new impetus in 1991, as the trade between the U.S.S.R. and East-Central Europe is collapsing. Second, a major restructuring of the economies is taking place. Manufacturing plummeted the worst, while agricultural production diminished relatively little, and trade grew substantially. Third, inflation is the outstanding problem. Two countries (Poland and Bulgaria) suffered from three-digit inflation, while the rest had two-digit inflation.

Fourth, unemployment is a surprisingly small problem to date. In fact, four out of six countries are still having overfull employment of 2 percent unemployment or less.

1. The obvious conclusion from this cursory review of the statistics is that inflation is the key problem that should be fought at virtually any price. If we turn our attention to the three most reformist countries--Poland, Hungary and Czechoslovakia - the problem appears rather curious from an ordinary Western point of view. All three had balanced state budgets in 1990. Monetary policies were reasonable and responsible. No major labor market problems occurred. One major source of inflation was the abolition of subsidies, another falling terms of trade. However, the really worrisome aspect of this inflation is that money is generated at the enterprise level, as state enterprises do not pay each other, but are not forced into bankruptcy. In Janos Kornai's words, their budget constraints are soft. Thus, it is necessary but not enough to pursue strict financial, monetary and incomes policies. In addition, bankruptcy procedures must become effective. As a consequence, a substantial increase in unemployment will have to be accepted. It appears natural to compare with Spain in the 1980s, where unemployment hovered around 15-20 percent. In fact, the East-Central European economies are still to be considered overheated.
2. One necessary condition for the accomplishment of hard budget constraints in enterprises is privatization. Otherwise, political criteria will continue to supercede economic criteria; no true independence of enterprises will arise, and they will neither compete nor innovate; nor will any Schumpeterian creative destruction take place; capital markets cannot become effective if private ownership is not dominant. This appears to be technically and politically the most difficult problem.
3. Another problem connected with the need for stabilization is the extraordinarily poor statistics. There is little understanding of what is actually happening in the economy. In particular, the declining state sector has long been exaggerated in the official statistics, while the growing private sector has been understated. Similarly, industrial production - which is falling most - is measured most attentively, though it means little to the standard of living. Retail trade and consumer services, on the contrary, are chronically underassessed. State enterprises want to boost their production figures in order to attain plan targets, while private enterprises prefer to conceal their achievements to evade tax. Previously, there was no effective control of quality, which has invariably been exaggerated. The price system was completely distorted. Prior shortages brought hardships and "real" incomes could not be exchanged for desired commodities and services. Forced substitution lowered the actual standard of living. A lot of sheer wastage was recorded as net production. In addition, sampling techniques have rarely been used. While it is plain that the suffering of the population is much less than the official statistics suggest, it is difficult to establish how much less it is. The statistical discrepancies may be startling. It

must be a top priority to improve statistics so that a proper picture of the development of the economy may be drawn. In the meantime, it seems wise to focus on combatting inflation, neglecting apparent declines in production and increases in unemployment, as major structural changes are necessary. However, such a course will require a great deal of political courage, as most people and politicians alike tend to believe too much in official figures. A suitable starting point should be to consider communism as an economic disaster. Invariably, the performances of communist economies seem to have been exaggerated both in the East and the West. If sufficient severity is not pursued, unbiased and dangerous calls for looser monetary and fiscal policies are likely to be heeded. As a result, hyperinflation may erupt, and "Argentinization" may ensue.

4. One important question to which surprisingly little attention has been devoted to date is the economic role of the state. Ironically, the all-embracing communist state failed miserably to perform all the basic functions of the state. It is not so surprising, because with the process of decentralization in the old communist system, power filtered down to the branch ministries and enterprise directors with little interest in the long-term, common good. Thus all kinds of infrastructure were increasingly neglected. Now, the basic functions of the state must be restored as soon as possible. First of all, in the face of blatant corruption and criminality, law and order must be reinforced, which requires the restoration of the legal system. Secondly, the state must establish the foundations of a proper financial and monetary system (though leaving as much as possible to the market). Thirdly, the state must assure society of some basic social insurances and facilitate the establishment of a modern infrastructure, notably telecommunications. However, the old state apparatus is singularly badly suited to accomplish these tasks. Its main task has been to administer the economy, and its communist cadres are utterly demoralized, wrongly trained and frequently hostile to the new liberal society they are supposed to build. The capacity of the state will be strictly limited for long also because the state administration will be preoccupied with its own restructuring and tax revenues are bound to decline sharply in the transition period. One obvious conclusion is that the state administration must get out of the enterprise sector just as fast as possible and return to basics. A basic requirement of a civil servant should be an oath to the new democratic constitution. Preferably, a whole new civil service should be created through the recruitment of young university graduates through open, competitive exams, which would be followed by good training. By creating such a corps, a new esprit de corps could be aroused as *École Nationale d'Administration* did in France after the Second World War. Besides, it is vital that senior civil servants are reasonably well paid for the strengthening of their morale.

TABLE
Economic Key Indicators, 1990
(Preliminary official figures,
annual increase in percent)

	National Income	Industrial Production	Agricultural Production	Inflation	Unemploy- ment
Poland	-13	-23	-1.4	344	6.5
Czechoslovakia	-3.1	-3.7	-3.5	10	<1
Hungary	-5	-5.0	-7.0	29	2.1
Bulgaria	-11	-10.7	-3	184	1.9
Romania	-11	-20	-3	---	2
USSR	-4	-1.2	-2.3	19	4

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The history of economic thought is one mainly of incremental advances. Giants such as Smith, Ricardo, Walras, Böhm-Bawerk, and Pareto, or Keynes appear with disappointing infrequency. All these men, it is worth noting, were men of their times and their contributions to economic analysis germinated in the practical economic issues of the day.

Today, as ex-socialist countries attempt to "marketize" their shattered economies, we have another set of economic issues that is producing a major new development in economic thinking: The Political Economy of Transition to The Market. It is a development that has yet to find its Smith or Ricardo. Perhaps it never will. Perhaps a new body of economic theory will simply emerge from the experience of newly legitimate governments of Eastern and Central Europe as they grapple with the exigencies of circumstance. I would argue that the foundations of this new theory (if it is new) are already before us; the Political Economy of Transition is already alive and growing. Making no pretence to rival the giants of yesterday, let us try to summarize some of the most important lessons that seem to have emerged from that experience and couch them as recommendations to new post-communist governments.

1. Strike While the Iron is Hot.

Post-communist governments coming to power as the result of free (or nearly free) elections follow oppressive and profoundly unpopular regimes. After their elections, if those are genuinely democratic, the new governments normally enjoy a period of popular hope and support that can be used to make the maximum progress in the direction of democratic politics and market economics. Unfortunately, that period is likely to be fairly brief because popular expectations of early improvement in living conditions are impossible to fulfill.

Judging by the caution that they often display, the new political leaders appear not to appreciate the intense nature and probably short duration of their "honeymoon" with public opinion. The reality seems to be that, if they did, they could push through strong measures to build the foundations for the market economy. Such firm and resolute action taken during the honeymoon may, counter-intuitively, earn popular respect and enhance the leaders' political prospects more than indecisive evasion typical of more timid leadership.

2. Be Prepared, Nonetheless, for Political Self-Sacrifice.

Political power is likely to rest on shaky social foundations in the immediate post-communist period. Political parties will be amorphous and weak while political power will be exercised by relatively small collections of individuals grouped around leading personalities.

As overblown and unrealistic expectations are disappointed, popular disenchantment will ensue and political support for the new leaders will ebb. Consequently, the first post-communist governments are likely to be fairly short-lived. With slim prospects for long incumbencies, the leaders of those governments should proceed boldly to implement the policies necessary for creating market economies in the expectation that history will remember them favorably even if the voters do not. This advice, which may seem tantamount to courting political extinction, is the hardest advice of all for politicians to accept.

3. Burn The Bridges Behind You.

Because the "honeymoon" cannot and will not last, it is vital that the most be made of it. That means that the new leaders should act quickly and effectively to block a retreat to the old system. That means that recommendations 5 to 10 should be implemented rapidly and radically.

4. Have Strong Economic Leadership.

Where the top political leadership has not included a strong individual (such as, e.g., Balcerowicz or Klaus) who understands what must be done, and/or where the primary responsibility for forging and executing transition policies is diffused and ill-defined, the prospects for transition are poor. In other words, a resolute and focused leadership is necessary to achieve a rapid and relatively painless transition.

Strong economic leadership means knowing where and how to move ahead but it also means having the ability and patience to communicate effectively with leadership colleagues, parliament, and the public. This seemingly obvious point appears to be inadequately appreciated in Central and Eastern Europe.

5. Privatize, Privatize.

The most effective barrier to retreat is a strong private business sector. Basically, only two ways exist to accomplish this. First, do everything possible to stimulate entrepreneurship (see Recommendation #9). Second, move enterprises and other assets into the hands of real owners as quickly as possible.

Before the private sector can go far, however, the uncertainties and confusions surrounding property ownership must be cleared up. That means, above all, that the

issue of restoring ownership to previous (pre-communist) owners or their heirs must be faced and, to the maximum extent, resolved. As the experience of every nation that has begun the transition shows, this is an issue that cannot be swept under the rug or waved away because it is troublesome. Naturally, the issue presses less urgently the more remote historically were the illegitimate Bolshevik confiscations.

As soon as it is possible to transfer clear titles of property ownership to private owners, energetic privatization should begin. This applies with particular force to small businesses: retail shops, restaurants, service establishments, etc. A not inconsequential reason for moving quickly with "small scale privatization" is that a quick and positive supply response can be expected in this sector, a response that will provide early benefits to a populace otherwise enduring considerable discomfort attendant to the transition. Additionally, such a step is an example of burning the bridges to retreat.

6. Liberalize Prices Sooner, Not Later.

The longer the old administered system of pricing remains even slightly intact, the more difficult it will be to rationalize all other parts of the economic system. Controlled prices mean markets in disequilibrium, distorted resource allocation, budget-busting subsidies, and the other all-too-familiar pathologies of degenerate socialism.

The nettle of rapid and comprehensive price liberalization must be grasped. Plenty of political courage and political strength are required to do it. Populist howls will rend the air. The government's political life may be threatened. But price liberalization is another hard-to-reverse step that will earn a new government a respected page in the history books. The adverse impact of such measures on pensioners and others on fixed incomes should be ameliorated by direct income adjustments or subsidies.

7. Create a Stable Currency.

Newly elected governments in ex-socialist countries invariably inherit disastrous currency systems. Monetary emissions will be out of control because the previous government will have resorted massively to the printing presses to cover burgeoning budgetary deficits. The central bank will likely be a pawn of the finance ministry. Little economic recovery will be possible until this situation is corrected.

The new government can give its people nothing of greater value than the foundations for a stable currency. That means, at a minimum, that the source of monetary emissions must become far removed from the control of the finance ministry or whoever else must fill the gap between state budgetary revenue and expenditures.

Beyond that minimum, but extremely desirable, should be a constitutional requirement that the government should live within its means, i.e., that its revenues should balance its expenditures. If, temporarily, the state budget should find itself in

the red, then the deficit should be covered by government debt obligations that cannot serve as reserves for the banking system.

Bolder, but highly desirable, would be the decision not to introduce a fiat currency at all but, rather, to create the closest possible equivalent to a metal-based currency system. The world already has too many so-called "central banks" that are little more than inflation generators. Much better it would be to base the new currency on a basket of convertible currencies such as the ECU.

8. Impose a Hard Budget Constraint Everywhere.

Even the most aggressive possible privatization policy will not divest the state of its ownership of all economic enterprises. The state sector, with a considerable number of state-owned enterprises, will remain an unfortunate feature of the economic landscape for some years to come.

Even though some enterprises remain state-owned or cooperatives, they should be subjected to the same financial discipline as that applying to private firms. In other words, state enterprises and cooperatives should not be bailed out by direct or indirect subsidies, artificially easy credit, coddled monopoly, or any other kind of governmental favoritism. Those state enterprises and cooperatives that can survive on a "level playing field" will have achieved a kind of economic legitimacy. Those that cannot should pass through bankruptcy to receivership with appropriate disposition of assets. Only the credible threat of bankruptcy is likely to bestir the managers and workers of many state enterprises to behave in a socially productive manner.

9. Establish the Legal and Regulatory Basis for the Market.

The first step is to closely examine the body of inherited law and regulations and purge all parts of it that restrain and inhibit the private sector. Since a major purpose of socialist law was to de-legitimize private enterprise, much of that law must be discarded and replaced.

A new body of law pertaining to commerce, banking, insurance, foreign trade, business formation, regulation, etc. must be created. Do not try to re-invent the wheel; use the law of a nation with a successful market economy as a model to be studied and emulated where appropriate. Strive to make these new laws compatible with world standards and, more specifically, the laws prevailing in the economic space to which the nation aspires to become a member (e.g., the EC). What applies to the law also applies to accounting and other business standards.

De-regulate as soon as possible, and keep governmental regulation of business simple and at an absolute minimum.

10. Liberalize Foreign Trade.

Convert all quantitative trade barriers to tariffs and begin a brisk schedule of tariff reduction whose aim is to totally liberalize trade within, say, three to five years. The consequent integration into the world economic system is to be greatly welcomed as is also the competition that foreign suppliers will afford to monopolistic domestic producers.

Move in brisk stages toward total convertibility. Begin by making the domestic currency internally convertible, i.e., permit citizens to buy, sell, and hold any currency in any amounts. Permit the rate at which domestic currency trades for foreign currency to find its own level in the market and keep official interference to, at the most, a "dirty float." Strive for convertibility on capital account within a decade or less.

Encourage direct foreign investment by creating a business climate that is friendly to all private enterprise, domestic as well as foreign. Do not extend subsidies or other special favoritism to foreign investors. If the business is attractive to domestic business, then foreigners will perceive that to be the case and also be attracted. This advice does not, however, preclude aggressive marketing of the nation's genuine attractions to prospective foreign investors.

Conclusion:

The preceding pages have presented ten pieces of advice that seem to flow from the experience of successful market economies throughout the world. More specifically, they flow also from the experiences of those Central European nations that have embarked on the transition to market economies. Looking them over, one observes that many of them are similar to the advice commonly given developing countries and seems a bit presumptuous to insist that they flow from a novel "Political Economy of Transition to the Market." However that may be, the advice seems to be withstanding the test of time and experience. That merits its careful study.

V. INTEGRATION INTO THE INTERNATIONAL ECONOMY

Highlights and Commentary

Integration into the international economy involves the liberalization and expansion of trade, opening to foreign investment, participation in international economic institutions, creation of capital markets, and movement toward full currency convertibility through meaningful exchange rates. Integration is both a transformation objective and a result of domestic economic transformation: economic liberalization, monetary stability, and openness can lead to greater inflows of technology and capital as well as exposure to competitive world standards; this contact with the world market should in turn accelerate further opening and integration. In this interactive process, technological innovation is central. Domestic transformation, together with opening to the world economy, will create an environment that stimulates technological change and modernization.

A foreign economic strategy must balance, however, the benefits of integration with the costs of exposure, competition, and interdependence. Furthermore, successful integration may depend as much on actions by external actors, in particular the developed market economies and international institutions, as on actions taken by the governments of the transforming countries.

The representatives of international economic institutions emphasized that the availability of external assistance will depend on a clear commitment to comprehensive democratic and market reforms. Specifically, IMF and World Bank lending is based on conditionality explicitly linked to policy change and implementation. By joining these organizations (including the OECD and the GATT) and receiving assistance, a member country accepts the process of conditionality and surveillance over its progress.

Although, as Harald Malmgren noted, the conditions imposed by international institutions represent a "framework of constraints on national behavior," they carry political and economic benefits for the recipient country as well. First, commitments made with international organizations can provide governments with an external tool for overcoming particular domestic pressures in order to enhance trade and openness. Second, in developing the programs and conditions to guide assistance, the international organizations bring broad experience and expertise to bear on the specific problems of the member country. Country studies, such as the ongoing OECD study of Hungary, offer not only professional assessments of economic performance and problems, but also can help to develop domestic statistics and analytical capabilities for continuing assessment of a country's transformation. Finally, participation in international organizations and adherence to their requirements can be a catalyst for gaining assistance from other sources, especially the private sector.

Among the international institutions that offer both widely accepted criteria for assessing performance and assistance in the process of transition, the Conference on Security and Cooperation in Europe (CSCE) has a special role. CSCE alone comprehends the full spectrum of issues involved in transformation -- political, economic, human rights, and security relations -- and thus is uniquely positioned to guide and support Central and Eastern European integration. Established as an ongoing process in 1975 for the purpose of bridging East and West, it is a forum in which the Central and Eastern European countries along with the countries of Western Europe, the United States and Canada participate as full and equal members. The interrelationship of political and economic reform was strongly reinforced at the CSCE Bonn Conference on Economic Co-operation in Europe (April 1990) which adopted concrete norms for encouraging trade, investment and economic cooperation among the member countries. Using the Bonn Document, in particular, as a standard, the CSCE should continue to monitor and encourage the implementation of CSCE commitments relating to trade and investment conditions in all member countries. Moreover, the CSCE, to the extent it develops and fosters interparliamentary dialogue, could be an especially effective avenue for the exchange of experience on developing the legislative bases upon which foreign economic policy is formulated. The CSCE can also provide useful guidance to the work of the United Nations Economic Commission for Europe (ECE) which can play a meaningful role in the conduct of commercial relations.

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Béla Kádár
Minister of International Economic Relations
Republic of Hungary

Due to the small size of its domestic market, geopolitical situation, scarce endowment with natural resources, as well as historical heritage of its economic development, Hungary is in heavy reliance on international economic relations. The openness of the economy is shown by the fact that the ratio of exports to the GDP has traditionally exceeded one third. As a consequence, the country's economic progress is closely linked to the performance of its external economy and to its integration in the world economy. Hence, for Hungary it is no option but a fundamental necessity to get involved, as fully as possible, in the system of international economic relations.

In the development of international economic relations a key role is played by international economic organizations. Among those of outstanding significance are the institutions considered as the basic pillars of the post-World War II system of multilateral economic co-operation, i.e. the GATT, the IMF and the World Bank.

In evaluating the benefits of participation in international economic organizations not only the various concrete advantages, i.e. credit sources, tariff concessions, improved market access conditions, should be considered. It is equally important to have possibilities for participation in and contribution to the process of regulation and development of economic processes, as well as of representing the country's interests. The operation of international economic organizations provides for a continuous exchange of information, which on the one hand promotes the creation of harmony between the national economic policy and the international standards and, on the other hand, contributes to the formulation by our partners of a realistic picture about the situation of the Hungarian economy and the trends of its development.

The importance of participation in international economic organizations has been recognized a long time ago. However, in this connection, account should be taken of the fact that a great part of these organizations are not automatically open to those showing interest. Participation requires the undertaking of commitments. Given that the set of regulations established by these organizations for international economic relations are tailored to market economies, Hungary's involvement has become viable to the extent that its internal economic development has grown mature for that and as it has been made possible by domestic and international political conditions.

It is not accidental that Hungary's accession to the GATT in 1973 became possible after the introduction of economic reforms in 1968 and in the period of détente of East-West political relations. The General Agreement on Tariffs and Trade, although formally being no organization but an agreement functioning with a temporary character since 1947, is an international forum determining the fundamental rules of the game of world trade.

As a small country heavily relying on international trade, Hungary is strongly interested in the existence of a stable and predictable multilateral trading system based on effective principles and rules. In fact, such a system -- even though its primary formers are the countries playing a cardinal role in the world economy -- protects the weaker countries having poor bilateral bargaining power from arbitrary and unilateral measures.

The active participation of Hungary in the activities of the GATT has promoted the development of Hungarian trade policy instruments in accordance with the internationally accepted and applied rules. As an example, the Hungarian nominal average tariff rate of 32 percent before the accession to the GATT has been decreased as a result of successive tariff negotiations to 16 percent by the end of 1990. The GATT is also an important forum for Hungary to represent its external economic interests consistently and to take a stand against the trade-restricting measures applied by its partners vis-a-vis Hungary.

As regards the involvement in the system of international financial relations, an important milestone was Hungary's accession to the IMF and the World Bank in 1982.

Until the end of 1990, the total amount of stand-by and other loans provided by the IMF to Hungary amounted to SDR 1.3 billion. In the same period, 23 projects were financed by the World Bank with a total amount of US\$ 2.3 billion. These programs aimed at facilitating structural adjustment, development of industrial and agricultural production and modernization of infrastructure. Hungary joined the International Financial Corporation in 1985 and last year became a member of the Multilateral Investment Guarantee Agency. Participation in these institutions not only made it possible for the country to obtain additional resources necessary for the development of its economy, but also played a decisive role in forming the international financial community's view on Hungary. It also meant that from the 1980s, the shaping of Hungarian economic policy was being closely monitored by the international financial institutions.

Hungary's relations with the international economic organizations entered into a new phase with the change of the political system and the economic model. In order to achieve a market economy, an international economic environment supportive to our internal efforts is indispensable. In shaping and maintaining this, an important role is played by international economic organizations.

As regards trade, multilateral negotiations under the auspices of GATT, known as the Uruguay Round, are currently underway. The success or the fiasco of the negotiations, being the most ambitious yet in the history of the GATT, will exercise a decisive influence on the future conditions of international trade. The Round may be brought to a successful end only if all negotiating parties are fully aware of their responsibilities. In this respect a specific burden lies with the most important actors of the world economy. Hungary, within the limits of its possibilities, will do its utmost to promote a successful outcome of the negotiations. The resulting strengthened multilateral trading system, more effective international disciplines and the gradual reduction or elimination of market access barriers would greatly facilitate the success of the Hungarian efforts to liberalize its economy, open up to the world economy and to be even more completely integrated in world trade.

Hungary's participation in international organizations helps our partners to get a full picture of our steps already made towards a market economy, as well as of the directions of further actions. Beside providing information, we consider it very important to get feedback from international organizations and to learn from the experience of other countries, which we can utilize in the course of economic transformation. In this respect, mention should be made that within the framework of the GATT trade policy review mechanism, Hungary's commercial and economic policy -- based on a voluntary undertaking and as the first from among the Central and East European countries -- will be the subject of an examination in April, this year. The country study to be prepared by the OECD on Hungary may also be a useful piece of assistance. For this purpose experts from the organization visited Budapest this week and conducted discussions to obtain the necessary information.

Our favorable relations with the international financial institutions are characterized by recently concluded agreements, as well. The structural adjustment loan provided by the World Bank last year (a second package is under preparation) and the three year extended arrangement (with a value of SDR 1.1 billion) recently concluded with the IMF may be of great assistance in the consistent implementation of economic transformation. From the Hungarian side we appreciate the establishment of the European Bank of Reconstruction and Development and we look forward to its activities.

The political and economic changes taking place in the Central and East European region cause not only the individual countries, but in many cases also the international organizations to re-evaluate their role, practice and fields of activity. Considerations which have already been given to the adaptations to the new situation are manifested in the concluding document of the CSCE Bonn economic conference and in the decision of the UN Economic Commission for Europe setting five priority areas (namely statistics, transport, environment, economic analysis and trade facilitation) for further action.

The political and economic changes -- besides the above stated -- make it possible for Hungary to establish new relationships with other important international organizations and integrations of the developed market economy countries. In the spirit of this endeavor, Hungary wishes to take part in the activities of the OECD and as the necessary conditions are met, to become a full member of the organization. Also, negotiations are under way on the establishment of an association agreement with the EC and free trade agreement with the EFTA.

Following the aim of full integration into the world economy, the Hungarian external economic policy intends to strengthen relations with the international economic organizations, taking an active part in their activities. At the same time we expect these organizations to form an objective picture of the results and problems of Hungarian economic development, and, on this basis, to show appropriate receptivity with respect to rendering assistance to the Hungarian economic transformation.

Harald Malmgren
President, Malmgren Associates

Multilateral economic institutions and trade arrangements, and their associated international rules and obligations, provide a framework of constraints on national behavior, and therefore constraints on national parliaments. These international institutions and trade arrangements are based upon negotiations among governments, and when the government of a nation joins, it voluntarily accepts a variety of limitations on its future freedom of action.

In the case of assistance by the IMF and the World Bank, a government seeking help must agree to implement specific economic policies, as a condition of assistance. Moreover, IMF participation requires adherence to IMF rules, including a variety of prohibitions on policies which distort trade, payments, and exchange rates of individual nations. In the GATT, the nature of constraints is somewhat different: The GATT does not provide financial support. Instead, the GATT is a framework within which various governments of the world negotiate trade policies with each other, making mutually binding commitments to liberalize access for imports and to avoid trade-distorting policies such as export subsidies, and binding commitments to avoid discriminatory treatment of the goods and services of one nation over those of another. If a government wants to act inconsistently with its negotiated commitments, other governments are free to seek compensation or take retaliatory action, in order to rectify the situation arising from unilateral breach of commitments by the initiating government.

Similarly, within regional economic groupings, and especially free trade areas and customs unions, governments cannot act unilaterally without opening the possibility of offsetting, or retaliatory, action by other governments.

It is important for parliamentarians of the nations of Eastern Europe and the U.S.S.R. to understand that these internationally agreed limitations do operate as constraints on national parliamentary action. Most parliamentarians in the Western, or market-oriented, economies do not object to such constraints. On the contrary, most parliamentarians feel that these internationally imposed restrictions on freedom of action protect individual parliamentarians from undue or unwise domestic political pressures.

All parliamentarians are continuously subject to direct pressures from interest groups within their home constituencies, and within their own regions and nations. Economic pressures tend to be highly specific, relating to individual enterprises, or groups of workers or farmers, or particular villages and towns. But the desires of individual groups often run counter to the broad interest of nations as a whole. To protect themselves from undesirable specific, local pressures, parliamentarians often welcome the existence of internationally agreed restrictions which can be explained as limiting the freedom of action of individual parliamentarians.

Thus, since the late 1940s, most governments of the market-oriented economies of the world have found it convenient to join and adhere to internationally negotiated and agreed systems of economic rights and obligations. Most parliamentarians have welcomed and supported these internationally agreed frameworks which limit the freedom of action of parliaments to take unilateral economic action affecting other nations.

Within broad geographic regions, there have also been efforts to bring together the disparate trade and economic policies of neighboring countries, to facilitate opening and

expansion of contiguous or nearby markets. The most notable development has been the creation of the European Common Market, and its gradual expansion and evolution into the European Community (EC). Alongside the EC has been the emergence of the European Free Trade Agreement (EFTA), encompassing smaller West European countries not politically linked to NATO and western security policies, including the Scandinavians, Switzerland, and Austria. The EC and EFTA have negotiated special arrangements for trade between these two groups, providing for essentially free trade and the emergence of the largest single marketplace in the world.

These kinds of regional groupings usually aim to unify, or at least harmonize, business laws, property laws, and other laws affecting commercial business and private financial activities. Ultimately, this process of bringing national laws and regulations into convergence assures the widest possible latitude for businesses to operate in a maximum market area. It also reduces the political quarreling within individual nations over business and private property laws, by posing uniform, transnational frameworks into which national policies and laws must be fit.

In this way of thinking, it would be reasonable for the emerging economies of Eastern Europe to consider the development of some common economic institutions and commercial understandings regarding their mutual economic relations, but especially regarding the shaping of national laws regarding business property, commercial law, protection of intellectual property, treatment of foreign enterprises relative to domestic enterprises, trade policy, etc. In other words, since the emerging economies of Eastern Europe are each developing entirely new laws regarding private property, business, and market-orientation, it would be sensible to explore the development of such laws together. If the parliament of each country in the region works separately and independently, the economic laws that will emerge will inevitably be full of points of conflict and inconsistency as between the various nations. This will discourage, and even block, the growth of economic relations. Moreover, the separate and incongruous development of business and economic laws in various parts of Eastern Europe, based upon differing local political pressures, will inevitably impede the opening of economic relations between these nations and the EC and EFTA.

Thus, it would seem highly desirable that there be some form of inter-parliamentary cooperation and coordination in the development of the business and economic laws among the emerging economies of Eastern Europe. This does not necessarily require negotiation of a free trade area, and certainly does not require establishment of a common currency or single central bank. Rather, what is needed is a more loose, cooperative approach among parliaments to begin devising the foundations for new, market-oriented economic behavior in the emerging Eastern European nations, separately and together.

Such cooperation and coordination among parliaments would also help individual parliamentarians to seek the "best" policies without being unduly influenced by specific, narrowly focused local political pressure groups, and by old, established economic

interests that are reluctant to allow modernization. Common laws supported by inter-governmental agreements would open the way for sound development of market-oriented policies, protected by mutual commitments to avoid trade-distorting, special interest policies which might harm each other's interests.

David Bock
Director, Operations Staff
The World Bank

It is an honor for me to be with you today and to address this distinguished group of parliamentarians from Central and Eastern Europe and other countries that have such a strong interest in this region.

The World Bank's association with Central and Eastern Europe dates back to 1945. Poland, Czechoslovakia and Yugoslavia were founding members of the World Bank, although Poland and Czechoslovakia subsequently withdrew only to join again in 1986 and 1990 as the process of economic transformation began in earnest. Romania became a member of the World Bank in 1972, Hungary in 1982 and Bulgaria in 1990. Albania has recently applied for membership.

World Bank lending to the region as a whole exceeds \$10 billion; lending to Yugoslavia accounts for nearly half of that total. Romania had received 33 loans for \$2.2 billion until it ceased borrowing in 1982. Lending to Hungary has been about \$2.5 billion. Over the last 15 months, the World Bank has invested more than \$1 billion in the economic development of Poland.

All of these loans are at market rates of interest and for maturities of 15 years or more. The creditworthiness of the borrower is a critical consideration in all World Bank lending, a point to which I will return in a moment.

Until 18 months ago, most of the Bank's lending financed long-term investments in infrastructure, industry and agriculture. Long-term financing for well-conceived and productive investment remains our basic business. However, we have learned from extensive experience, in all parts of the world, that good projects frequently fail because of inappropriate economic structures and weak government policies. Accordingly, during the 1980s, we began to develop new types of lending designed to encourage and support policy and structural change in the overall economy. One such loan was made to Yugoslavia in 1983 to support early attempts at reform there. In the 1986-88 period, several loans were made to Hungary to support the restructuring and reform of the industrial sector.

With the sweeping political and economic changes of the last two years, the level of World Bank activity in Central and Eastern Europe has increased dramatically. Major

loans in support of the transformation to a market economy have recently been made to Poland, Hungary and Yugoslavia. Similar loans are being prepared for the other countries. These loans are quick-disbursing and designed to finance part of the costs of economic adjustment. They are explicitly linked to policy reforms being undertaken by the country. We only lend when we are satisfied that the economic policies of the country are sufficient to ensure that the loan will contribute to economic growth and development.

The conditionality of such lending is frequently linked to legislative action. As a matter of principle, the staff of the Bank never deal directly with the parliaments of any member country. But it is quite common for the various tranches of policy-oriented loans to require the passage of key pieces of legislation--approval of a budget, for example, creation of new supervisory institutions, elimination of restrictive regulations, or simplification of the rules governing foreign trade.

All such lending conditionality is unique to the country concerned. We have learned from experience that the single most important factor in the success of such lending is the government's own commitment to the program or project being financed. We usually provide extensive assistance to the government in formulating such a program through careful, objective studies of many different aspects of the economy. These analytical studies help in designing specific investment projects as well as broader policy-oriented lending. And they are the main way in which we bring our worldwide knowledge and experience to bear on the specific circumstances of each member country.

Let me now briefly touch on a few of the lessons of experience gained thus far in the transformation of centrally planned systems to market-based economies, as they pertain to the integration of these economies into the international system.

First, reforms need to be quick and comprehensive. All of the economies in transition are plagued by inflation, and as Anders Åslund said yesterday, this is a very serious threat to the success of everything else the East and Central European governments wish to achieve. Controlling inflation is a matter of financial discipline throughout the system, and for the countries in transition this requires the rapid creation of new market-based mechanisms for enforcing financial discipline. Public expenditure reform, opening a monopolized economy to foreign trade, establishing currency convertibility, strengthening tax administration, restructuring individual enterprises, shifting much of the productive sector to private hands are all part of creating this new system of financial discipline.

Second, good quality legislation is critical. A market economy is essentially a set of rules and institutions, regulating the behavior of independent economic agents. The quality of a country's laws and administrative systems, including especially the protection they provide to private economic activity, will have a major influence on the success of the economy.

Third, establishment of an independent financial system must be a key priority. The financial system plays an entirely different role in a market economy than in a command-administrative system. Financial systems are extremely underdeveloped in Eastern and Central Europe. New banking institutions need to be created, and appropriate regulatory and supervisory systems developed. It is crucial that financial institutions be independent of both the government and the enterprises they finance in order to have a sound and efficient system.

Fourth, the market economy requires a substantially different system of social security. In the near term, social legislation needs to focus on a "social safety net" to deal with the unemployment that is created by imposition of hard budget constraints in various sectors of the economy, as well as other social concerns. Well-conceived "safety nets" have been shown to be crucial in sustaining popular support for the reforms. Emphasis needs to be on retraining and other employment services. Longer term, the whole array of social benefits will need to be adapted to the new realities of the marketplace.

Finally, let me say a word or two about financing. The ultimate test of any economic program is whether it succeeds in persuading private investors to risk their own funds in the economy's future. The large flows of public finance from Western countries are themselves a transitional phenomenon. They need to be treated as a scarce resource and used wisely to support the transition to reliance on private capital flows.

Val Koromzay

Director, Central and East European Division
Organization for Economic Cooperation and Development (OECD)

The Nature of OECD

The OECD is an intergovernmental consultative body whose present members are the industrial market economies of western Europe, North America, Japan, Australia and New Zealand. Its central purpose is to improve global economic performance through a process of co-operation and consensus-building. A few comments on the functioning of the OECD in general may be relevant as an introduction to the more specific issue of the role of OECD with respect to the economies in transition. Six points in particular seem to me to be essential for understanding the specific identity of OECD as an international organization.

First, the OECD deals with a very broad range of economic issues of both general and sectoral import. Indeed, it is easiest to specify the range of OECD concerns by a negative list -- only national defense and security issues are not dealt with.

Second, the work of OECD is carried out primarily through committees or working parties that are made up of experts and officials from the member countries who have specific responsibilities within their own governments for the economic policy issues taken up in these various OECD bodies. Thus, monetary issues are discussed by representatives from financial ministries or central banks; agriculture or trade issues by representatives of the respective ministries; foreign assistance or environmental issues by representatives of foreign aid and environmental agencies respectively. In this way, OECD committee structure in some sense replicates, at an international level, the structure of national administrations.

Third, the major role of the OECD Secretariat is to provide the committees with information and economic analysis on the issues that the committees choose to discuss. This work is often, but by no means always, subsequently published. It is true that, in addition, the Secretariat has a public information role -- as for instance in the regular issuance to the public of internationally comparable statistics.

Fourth, the actual discussions that take place in the committees and working parties constitute a sort of multilateral surveillance -- a process in which the aim is to achieve greater consensus and co-operation by the exercise of mutual, though restrained "peer pressure".

Fifth, in most spheres the objective aimed at in this multilateral surveillance is not to negotiate legally-binding agreements or treaties, but rather to obtain intergovernmental commitments that express policy intention in specified areas. In certain areas, however, such as for instance the liberalization of capital movements, governments do take on obligations with a legally-binding character through adherence to OECD Codes.

Sixth, this relatively flexible approach to achieving co-operation and consensus -- while of course not always fully effective -- does carry a surprising amount of weight in shaping economic policies. Experience has shown that these processes are most effective in situations (that arise quite frequently) where governments' "better instincts" are to move in a particular direction, but where doing so is politically difficult. In such situations, OECD discussions can help by developing stronger intellectual arguments for the chosen policy course, by demonstrating that such policies command international support, and -- where the recommendations are published -- by providing a "credible witness" in favor of such policies.

OECD in Relation to the Countries of Central and Eastern Europe

Turning to the role of OECD in Central and Eastern Europe, the framework for this was created in May of last year when OECD members decided to create the Center for Co-operation with European Economies in Transition (CCEET). The Center was established to develop, through close consultations with the governments of Central and Eastern Europe (and subject to the agreement of the OECD's governing council) a

program of activities that would be responsive to the particular needs of those countries taking on the unprecedented challenge of moving from state-dominated systems of economic management to market economies. The Center is also directly responsible for co-ordinating the implementation of these agreed activities.

A particular point about the structure of the Center is that it is relatively decentralized. At its core is an administrative unit headed by the Assistant Secretary General who is responsible for overall planning and co-ordination. The substantive work is carried about by Secretariat staff -- most of whom are funded through the Center -- but who are physically located in various directorates that make up the Secretariat. There are pros and cons to such a decentralized structure, but at least two positive features stand out.

First, the work that is carried out in implementing the programs for Central and Eastern Europe remains in the overall framework of work that is carried out in various parts of the house on OECD countries. There is no fundamental break in the perspective from which issues are viewed depending on whether it relates to OECD countries or the countries of Central and Eastern Europe.

Second, because the directorates are the prime conduits between the Secretariat and the various committees of the OECD, this arrangement serves to maintain links between the work undertaken by the Center and the various OECD committees and should permit, over time, an integration of the work program of the Center into the work of the committees.

Early this year, the OECD decided to create, within the CCEET, a special program called Partners in Transition (PIT) whereby those countries that have made progress in their transition to the point where they could benefit from more intensive co-operation with OECD could be enabled to do so. Hungary, Poland and the C.S.F.R. are at present engaged in this program; detailed programs are presently being developed with each of these countries.

Some Aspects of the Work Program

It is not feasible to provide here a detailed account of the substance of the work that OECD is doing through the CCEET, but a few points can be highlighted.

First, it should be noted that, unlike the other International Organizations present at this seminar, the OECD is not involved at all in providing or channelling financial resources to the countries of Central and Eastern Europe. It is not set up for this.

Second, what the OECD does provide is technical assistance that is, at least potentially, as broad in scope as the work of the OECD itself, ranging from such general issues as clarifying options for tax reform, for the development of financial markets, or indeed for the conduct of macro-economic policies, to specific assistance in

drafting a competition law, setting up a job-placement agency, restructuring accounting or statistical systems, or developing a capacity for environmental monitoring.

Third, with regard to technical assistance, the comparative advantage of OECD derives in part from the breadth of issues that it deals with. Beyond this, there is the fact that assistance is not limited to the expertise of the OECD Secretariat; through the committees, national experts can be mobilized in relevant areas. The most characteristic feature of OECD's technical assistance is that it provides a range of perspectives, and alternative approaches to specific or more general policy problems reflecting the diversity of solutions that are compatible with market economies. In this sense, OECD provides the countries of Central and Eastern Europe not with a blueprint or single model of how to reshape an economy along market lines, but rather with a range of alternative arrangements and an understanding of the conditions favoring one or another solution. At a more fundamental level, however, the OECD perspective is not that one can pick market-oriented institutions like from a menu--one from column A, two from column B -- but that one has to focus above all on the inter-relationships among the choices and the coherence of the whole.

Fourth, I would like to mention one particular activity that is integral to the work with each of the countries involved in the PIT program: the preparation, on a regular basis, of assessments of overall economic situations and policy frameworks in each country, and of how selected key transition problems are being managed. A benchmark study of this sort is currently being undertaken with respect to Hungary, with a similar study soon to begin for C.S.F.R., and for Poland in the autumn. These studies are to be the basis for country reviews, where the prospects and policies of the country under review are examined within the OECD through a discussion between the country representatives and the representatives of the OECD countries. This is an illustration of the multilateral surveillance aspect of OECD, along the lines indicated in the beginning of my comments. Subsequent reviews will provide a means of systematically monitoring the transition process in the PIT countries.

Concluding Comments

I would like to end this presentation with three concluding comments. First, the OECD countries are strongly interested in assisting the countries of Central and Eastern Europe in making a successful transition to market economies: the creation of the CCEET and the establishment of the PIT programs are evidence of this.

Second, there is considerable flexibility in the OECD approach to co-operation with the countries of Central and Eastern Europe. There is the possibility of developing intensive interaction across a broad range of areas, or alternatively of focusing on a few specific points. Which of these is to develop depends on the speed and determination with which the countries concerned pursue the transformation process. The relevance of OECD to the countries of Central and Eastern Europe clearly increases in line with

the relative importance of market mechanisms and related market-based systems of macro-economic management in these countries.

Thus, finally, there is -- despite the flexibility of the OECD approach -- a kind of conditionality in relations between the OECD and transforming countries. This is not a conditionality as defined by precise performance criteria -- such criteria are not really relevant since, for OECD, there is no financial counterpart. But there is an element of conditionality in the recognition of the fact that deepening co-operation -- and indeed at some point on the road the possibility of membership -- entails a commitment to persevere with the difficult, complex and at times surely painful process of transition to a market economy if this co-operation is to make sense.

György Szapáry

Assistant Director and Resident Representative
International Monetary Fund (IMF)

The IMF has an obvious role to play in helping the Central and Eastern European countries transform their economic structure and, at the same time, cope with such immediate economic problems as inflation, external debt, and low growth. A fundamental objective of the Fund is to promote growth and an open multilateral system of trade and payments. In pursuit of this objective, the Fund encourages sound economic and financial policies and viable external payments in all its member countries.

The IMF's role in the Central and Eastern European countries, as in all other member countries, involves financing, policy advice, and technical assistance. The IMF conditions its financial assistance on the recipient country implementing policies that will correct its economic weaknesses and ensure a viable external payments position within a reasonably short period of time. Typically, the conditions include measures in the monetary and fiscal areas to strengthen financial discipline, an appropriate exchange rate policy, steps to liberalize the trade and payments system, and structural measures that enhance the supply responsiveness of the economy.

The Fund has responded promptly to the financial needs of Central and Eastern Europe. Fund supported economic programs are in place or are under discussion with all member countries in the region: Bulgaria, the Czech and Slovak Federal Republic, Hungary, Poland, Romania, and Yugoslavia. The IMF is extending some \$5 billion of assistance to these countries in 1991. It also acts as a catalyst in channeling to these countries assistance from other sources--e.g., from the EC, G-24 and the World Bank--and in participating in Paris Club and London Club discussions.

Technical assistance is another important aspect of the IMF's work in Central and Eastern Europe. The reforms will work only if new institutions are set up and existing institutional arrangements are improved. The Fund is assisting this process by helping these countries to improve the functioning of the central bank and the financial system; to reform the tax, foreign exchange, and trade systems; to establish adequate safety nets to protect those adversely affected by the reforms; to improve tax administration and expenditure controls; to improve the country's economic statistics; and to train economic policymakers through courses both in the country and at headquarters in Washington, D.C.

The countries of Central and Eastern Europe are facing a formidable task in implementing market based reforms to make their economies more efficient and equitable and thus satisfy better the aspirations of their people. The task has been rendered more difficult by an unfavorable external environment characterized by higher oil prices and an unexpectedly severe disruption to regional trade. In these circumstances, the support of the IMF, as well as that of other financial institutions and donors, plays a particularly important role in helping these countries to restructure their economies.

Dennis DeConcini

Senator, United States Congress

Co-Chairman, Commission on Security and Cooperation in Europe

Mr. President, Fellow Parliamentarians, and Distinguished Guests:

It is a privilege to be here today to share experiences and exchange views on the role of parliaments in shaping and developing national economic policy.

Anyone who follows the annual debates in the American Congress on this issue knows that formulating legislation which effectively reflects as well as shapes national policy in a democratically pluralistic society is an arduous exercise -- an exercise often animated by heated debate. Members of Congress spend many long hours not only trying to balance the conflicting interests of different constituencies, but also trying to reach meaningful compromises among themselves as they attempt to shape policy according to their respective political philosophies.

As spirited as these debates can be, however, we differ not so much in the premise upon which our national economic policy is founded as in how best to enhance and stimulate that policy. Whether Republican or Democrat, we believe passionately that free market principles driven by individual initiative are the strongest formula for a healthy economy. The legacy of our laws since America's founding two hundred years ago reflect a divergence of views on how government can effectively strengthen the free

enterprise environment. The pendulum has swung back and forth over the years between a policy in which government plays an active role in regulating the business environment, to the policy of the past decade which leans predominantly against a strong federal role. Time, as always, is the best judge of what works at any given moment in history. The American people -- and American business interests -- ultimately let us know when we should adjust our course.

Today, the countries of Central and Eastern Europe are faced with the challenge of not only rebuilding but also reforming their shattered economies. At this critical juncture, you, their lawmakers, have an invaluable advantage which history doesn't permit very often -- the freshness and the momentum of a new beginning.

The American poet, T. S. Eliot, wisely observed that "to make an end, is to make a beginning."

The citizens of Central and Eastern Europe have put an end to a system of government which denied them their right freely to explore the very essence of the human spirit, individual creativity. In today's modern world of huge, multinational corporations and complex technologies, we often lose sight of what it is which really ignites a healthy, competitive economy. Corporations were all born out of the dreams and ideas of individual men and women. Henry Ford's idea, for example, to mass-produce an inexpensive car led to the global Ford Motor Company. Here in Hungary, the Tungsram Enterprise which has just concluded a major joint venture with our own General Electric Company -- was born of an invention by an American named Thomas Edison -- an American who was free to bring his ideas to fruition.

It is this spirit which we, as parliamentarians, have been entrusted to protect, encourage and nourish. How well we carry out our responsibilities will be evident in the economic health of our respective societies. We share the common legislative tasks of debating policy alternatives, drafting and approving legislation, and overseeing its implementation by administrative agencies.

But those forging the transition to democratic and market systems have the opportunity to start afresh. The laws and policies agreed to by the parliaments of your countries will be central to the long-term improvement in domestic economic conditions and to further integration into the international economy. It will fall to you to establish and, in some cases reestablish, a firm legal framework which will guarantee private ownership, instill the confidence to take risks, and ensure the freedom to pursue competitive ventures and realize profits. Such legislation will be essential not only to promote free market economies at home, but also -- and very importantly -- to provide the political guarantee of a legal basis for doing business in the type of environment which encourages foreign investors and joint venture partners.

While each nation and parliament will fulfill these responsibilities in its own way, the CSCE process has a valuable role to play in providing guidelines and supporting the

difficult transition to pluralism, markets and integration. In April 1990, the CSCE Bonn Conference on Economic Cooperation produced, by unanimous agreement among the 35 participating States, norms and criteria for establishing an economic environment conducive to trade, investment and industrial cooperation. These commitments, which concretely recognize "the relationship between political pluralism and market economies," can serve as a foundation for legislative initiative in the European parliaments.

As the agenda of this meeting indicates, there are serious dilemmas involved in pursuing democratization and a free market, and difficult trade-offs that must be confronted in implementing economic reform. These dilemmas and trade-offs are the stuff of which parliamentary debate is made. The CSCE process can help to ensure that the end results conform with the path to greater international cooperation envisioned by CSCE commitments.

For example, among the conclusions reached by the participating States in Bonn, one of the most central to effective economic transformation was the affirmation of the leading role of private investment. Specifically the states agreed that:

While, in the period of transition to a market economy, public financial support to well-defined projects can serve as a multiplier in the framework of economic reforms, such intervention should not distort the emerging market mechanisms. The participating States agree that capital from private sources will progressively become the principal source of external finance.

Given this conclusion, the creation of a favorable climate for investment must be of the highest priority for the newly emerging democracies. And to create such a climate, the pace and content of legislation adopted by the national parliaments will be critical.

What are the elements of a favorable climate for economic cooperation and private investment? The Bonn Document suggests that a variety of conditions are crucial:

- The ability of businesses, regardless of form of ownership, to enter and operate on the territory of the member state on a non-discriminatory basis, including access to supplies, labor and domestic marketing avenues.
- Comprehensive, comparable and timely economic, commercial and demographic information. Cooperation is particularly necessary for developing statistics on external trade, capital movements, employment, transport, foreign tourism, environment, energy and other raw materials and industrial production.
- Protection of industrial, commercial and intellectual property rights on a non-discriminatory basis.

-- Market-oriented and stable economic policies based on a reliable legal and administrative framework. Some elements of this framework include fiscal, competition, bankruptcy, and insolvency legislation; company laws; arbitration procedures; investment protection; free transfer of capital and profits in foreign currency, accounting systems; free flow of information; entrepreneurial autonomy.

-- Market-determined domestic price mechanisms and movement toward currency convertibility. These goals are underpinned by reform of the banking system; creation of capital, labor, and foreign exchange markets; reform of the tax system; and transformation of public enterprises.

These criteria can be critical to formulating legislative agendas which reflect genuine reform programs. They can also serve as benchmarks for businessmen looking for investment opportunities, and for Western governments seeking to structure and direct assistance to projects that will have a "multiplier effect" on the transition efforts of the reforming countries.

Many positive initiatives have already been undertaken, in varying degrees, by the countries in transition. Important policy decisions designed to implement specific provisions of the Bonn Document have been made. For example, the countries of Poland, Hungary, and the Czech and Slovak Republics have made definitive moves towards the essential elements of privatization: namely, the end of state ownership; the acceptance of fiscal and monetary discipline and the restructuring of their enterprises to be more competitive. The continued implementation of these policy decisions -- backed by a solid legal framework -- will contribute to further confidence-building in foreign business and financial circles looking to these countries as prospective business partners and potential new markets. The CSCE can serve as an important on-going gauge of how well these policies are being implemented.

The Helsinki process of periodic implementation review, evaluation and building upon existing commitments has created an effective framework for dialogue and international accountability concerning agreements made by participating States. This tested cornerstone of the CSCE process must continue in a constructive yet candid manner in order to help ensure that the criteria set forth in the Bonn and other CSCE documents are, in fact, complied with. Parliaments should not forget that they can and should influence their national delegations at CSCE intersessional meetings to take positions designed to help achieve greater implementation of CSCE commitments.

In fact, you may wish to consider the formation of a parliamentary CSCE Commission along the lines of the U.S. Helsinki Commission of which I am Co-chairman. The primary focus of our charter is to monitor and encourage compliance with CSCE commitments by all participating States including our own. I would also add that the Chairman of the Commission, Congressman Steny Hoyer, will be participating in the CSCE Parliamentarian's meeting being held in Madrid next week.

Chairman Hoyer will be looking, in particular, at ways in which parliaments can contribute to the CSCE process.

In addition to the review process undertaken by the CSCE itself, another, more concrete avenue for monitoring progress is the United Nations' Economic Commission for Europe, the ECE. The ECE is a frequently overlooked but valuable resource of CSCE which plays a useful role in pinpointing specific aspects of economic reform where further action is needed. The ECE supplements the broader agendas of the larger international institutions by providing important studies on such nuts-and-bolts areas of cooperation as standardization and statistical information gathering.

The work of the ECE, coupled with the results of CSCE implementation review and intersessional meetings, can serve to complement and focus the agendas of other international institutions such as the OECD, the IMF, and the World Bank as well as the new European Bank for Reconstruction and Development. The actions undertaken by each forum when looked at as a whole should be utilized in a coordinated and effective manner. This will ensure the transition to free market economies as well as increased integration into the international economic and financial system.

In closing, I am pleased to note that at this seminar are representatives of some of the major international organizations which are actively engaged in assisting the economies in transition in a key area -- the development of a competitive economic environment. We also have in attendance representatives of the world's leading commercial lending institutions. Their presence is a mark of how far some countries in transition have come towards meeting their Bonn commitments. But the key to a successful transition to a market economy -- in the final analysis -- is not reliance on foreign financial and technical assistance, although we all support this. Nor will real economic reform be achieved through sentiment, as Lech Walesa has so frequently stressed. True economic reform will come through the development of a healthy environment for taking the initiative, making investments, and ultimately realizing profits -- an environment in which freedom and prosperity are interdependent and mutually supportive. That is the real dynamic of a market economy rooted in democracy. It falls to us, as lawmakers, to do our part in this process by providing both the legal framework and guarantees necessary to ensure that the creative energies of those we have been elected to serve, are continuously nurtured.

VI. TRADE AND INVESTMENT

Highlights and Commentary

While participation in international institutions is a significant component of integration, the transforming countries are also generally interested in promoting freer trade and attracting private foreign investment to support growth and modernization in Central and Eastern Europe. In the long run, modernization and competitiveness in these economies must rely on domestic investment and the stimulation of domestic R & D. In the short run, however, while domestic savings rates are low and links to global markets insufficient to produce wide-ranging technological innovation, foreign investment, technology, and official assistance will play an important role.

In spite of the substantial need for investment resources in the countries of transition, their availability may be restricted by the intense global competition for capital and by uncertainty regarding business conditions in these countries. Noting the crucial role of the parliaments in establishing the standards and mechanisms for predictable and profitable economic activity, representatives of the international business and banking communities offered consistent advice on actions the parliaments should take to enhance the prospects for trade and investment.

The establishment of equal conditions for domestic and foreign investment, based on international standards, is a central requirement. Foreign investors should have reliable access to labor, materials, and repatriable profits; at the same time, they should not be given specific, individual inducements or assured markets that favor them above domestic investors. The reduction of tariff and non-tariff barriers, convertible currencies, and competitive exchange rates are goals towards which each of the transforming countries should be working. A stable political and legal environment, including a transparent tax code and statutes which enforce an ethical business climate, must be the foundation on which economic development occurs. Fiscal and monetary stability, and a functioning commercial banking system are also necessary conditions for attracting international business.

While each of the Central and Eastern European countries is working in its own way to create these kinds of conditions, they are doing little to promote regional cooperation among themselves. Problems of bilateral trade with the U.S.S.R. were mentioned by several participants, yet, as Marie Lavigne noted, this is not the only factor in regional trade deterioration -- trade among the other Central and Eastern European countries is collapsing as well. Dr. Lavigne and others argued that the transforming countries should create among themselves new mechanisms for cooperative action and preferential trade treatment. Although all the countries express interest in joining the European Community (EC) or European Free Trade Association (EFTA), full participation is not likely to come quickly; regional trade should not be sacrificed in exchange for new relationships. This is a critical time to cooperate, as each country is

devising its trade-related legislation, to ensure some compatibility of standards and conditions within the region that will make integration easier, rather than pose additional obstacles to more open European trade.

Western governments can do several things to assist in Central and Eastern European integration into the global market. First, official assistance, targeted to urgent needs, is recognized as important in the early stages of transformation, when private foreign investors remain wary. Second, it is proposed by the Group of Thirty that the Western industrial nations help to establish export credit agencies in Central and Eastern Europe and to reinsure their guarantees through one of the multilateral agencies. Finally, as participants from both East and West noted, the outcome of the Uruguay Round negotiations under the GATT will have a significant impact on the region; in particular, the elimination of Western agricultural subsidies is critical for the competitiveness of Central and Eastern European agricultural exports.

From the perspective of the Central and Eastern European delegations, major issues of concern were the need for more foreign investment, increasing trade with the West and especially access to the EC, and conditions for Western credit. It was noted by one Hungarian that all of the countries of the region are competing for trade and investment with the Germans, who have much better conditions; moreover, in competing for Western credits, up until now, the U.S.S.R. has received favored treatment. The most appropriate method for establishing convertibility was also a subject of discussion, as the different approaches taken by Poland, Hungary, and Romania were contrasted but justified in terms of specific local conditions.

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Erno Pungor
Minister without Portfolio
President, National Committee for Technological Development
Republic of Hungary

Ladies and gentlemen, Mr. Chairman, in my paper today, I would like to provide you with a short description, a short picture of the effect of research and development in the economy of a country and how we do this in Hungary because significant changes have occurred in this area too.

Research and development has not received proper attention in socialist countries in the sense that they did not consider this as a creative component of the economy. I believe that, in this respect, in Hungary the state of affairs was poorer compared to the rest of the socialist countries. There were several reasons behind this. One of the reasons was that the market where our products were sold did not require high quality

products. Consequently, it was not in the interest of industry to develop the quality of our product. The other factor was that in Hungary there was a patent law provided by legislation. Consequently, the director-general of the company, the deputy director, the chief engineer, were those who contributed to patent operations and they were not interested in having new innovations to inventions. Instead they tried to make the best of the previous invention, trying to make money out of it for at least a period of 15 years. I would not like to elaborate on this any longer. I only would like to note that, from the point of view of the development of the economy of the country, it is of fundamental importance what kind of research and development activities are taking place.

In the recent past I was in South Korea and there it was possible to develop new technology under conditions where they had not had any universities after World War II for a certain period of time. So they decided to call their professors, to appeal to professors, of South Korean origin in the United States of America to go back to South Korea and work there. And I do not think it requires specific analysis if you want to illustrate the impact of the effect of this.

The basis of our R & D is the circle of professionals, experts. It is of less importance to what extent they are equipped with the proper facilities and equipment. So I would like to put away the misunderstanding according to which, in general, it is not possible to purchase the proper machinery, equipment, facilities and devices which are required for high standard research. The products, the facilities, the machinery and instruments available on the market in general are six to eight years old. So, they are no longer suitable for research activities. Consequently, if you are working in the area of research you have to develop your own equipment for the purposes of your research. Also, you have to study the various tools of research work abroad and in your own country, too. I know that there is a relatively small number of people who are capable or talented enough to become research workers if they only have the opportunity to train themselves, without having the possibility to collect experience. Therefore it is important that research workers should be able to travel around to see other places and other practices.

Innovation means a basis for technological development based on which the industry of a country can no longer earn only a few pennies on a product but they will be able to make a great deal of money on them. Therefore, it is in the fundamental interest of all the countries to develop the area of research by employing talented people. There has to be a proper training of cadres.

In Hungary, there were several criteria considered when the cadres in the research area were selected. There are a number of people who are working in the area of research but they are not capable of doing research properly. For the time being, there are about 33,000 persons in Hungary who make their living by working in the area of research and development. I have put it this way because I have said there were 33,000, so it would have been a wrong interpretation and a wrong way of expression

if I had said that these people are research workers. They are people working in the area of research but some of them are not capable, they are not talented enough to do research in the proper sense of the word. Basic research and education are the kind of activities which are focused at universities. The major area of these activities is the university. Universities undergo a period of transition these days. At a number of Hungarian universities it is being discussed how we can develop university education to put things in proper order there. The fundamental issue here is that university education should not be some kind of schooling on the university level, but instead at the universities we have to teach people how to work and how to think properly. How to think in a creative manner.

Another issue that I feel I have to touch upon is instrumentation. In Hungary in the middle of the 1970s, we launched a program of endeavors and efforts and partially it was successful. In other words, in place of the feudalistic type of distribution of instruments, by this I mean if you were a person in a high position, you could purchase instruments of higher value and as soon as you had a guest, you could show him what fantastic instruments you had available for you yourself. Now we replaced this program and we introduced a more expedient system for distributing these facilities but we could not say that this had reached the proper level. Since it was the end of the 1970s, we no longer had the proper amount of money for purchasing all the instruments and facilities which we required at that time. I also have to admit that, due to the international assistance we have received in the recent period of time, we have been able to make the first step towards automation. That is, computer facilities are available in the country to a greater extent as compared to the past.

As I said, research is a kind of activity which takes you toward innovation. As a result, innovation is something very interesting. Innovation compared to basic research requires 10 times the money which is required for basic research. Because of being poor, this area did not develop properly in Hungary. For the time being, we would like to accelerate the development of this area and in a few minutes I will come back and tell you how we re-organized this zone of development. Well, innovation has several phases, of course. There is a phase in which we arrive at some kind of a product based on the basic research results and this is to be produced. Incubators will have to be used for this purpose. These days the system of financing which is implemented by the Hungarian bank is such that we have to pay quite high interest rates if we want to take loans or invest money in this area. An idea was launched a few years ago according to which we wanted to bring in, to introduce, "innovation parks" here. Well, this idea was not successful. Instead of implementing this idea, we have launched another program. We have introduced the incubator system, which means that, in a small scale manner in smaller institutions, we tried to meet the tasks of innovation. We can provide money for 15-17 thousand research workers in Hungary so that they should be able to be successful in their work, and this should also bring about results. For the rest of them, we cannot pay the cost of research, so there are about 15-16 thousand research workers who cannot have, who do not receive the necessary amount of financial means to be able to conduct their research programs. So the adequate financial background for

research activities is not available. Therefore, these days, whenever I participate in an international negotiation, I make efforts to attract foreign partners to authorize our research workers for conducting research programs and they also provide the means for this. This is because it is not only our purpose to save this generation of research workers so they should be active in the future, but it is also our purpose to establish proper relations between our research workers and the institutions.

Now, how do we address the brain drain as a further issue? For the time being, 15-18% of Hungarian research workers are working abroad and they are performing quite well. We are proud of them. They report results to us about which we can say that, in fact, the peak of the iceberg is just excellent. The peak of the iceberg in Hungary is excellent. Now the question is whether we have lost these people or whether we have not. I would like to emphasize that they haven't been lost from our point of view because, during the time when they were abroad, they learned rather a lot. They get familiar with conditions in which they can work properly. And if they see that similar conditions would be available here, and I sincerely hope they will be available here within a short time, they will be ready to come back and we will make efforts to achieve this because it is in our proper interest to do so.

And now, may I speak shortly about how we reorganized the system of subsidization provided for the technical innovation system. Earlier, there was a certain amount of money which was shared by the institutes. So, the money that the parliament voted for at an earlier date was distributed on the basis of the power composition represented by the various institutions. The R & D zone is supported considerably by the state. According to some data, it is supported by up to 2.7-3%, but in actuality the assistance and support which we receive is significantly greater.

Due to the selectiveness of our statistical information system much could be said about technical development. Now, as regards factual costs, they are much less than the previously set 3 percent. If we devoted so much we could write off the whole intellectual basis of Hungary. What we would have to get as a return on our investment within 45 years time would be 4 to 5 times as much as we originally invested. As a result, the parliament ruled that from now on all state intervention in monies will be pooled into one place, that is, the National Development Committee. We have established a new system there which is characterized by the following:

First of all the tender is a public one. The money is only accessible through a tender. A bidding process. There are no monies which could be allocated on a personal basis. The tender is a continuous one that goes on on an annual basis, so we are not obliging anyone to come up with ideas that will earn them the money. The links of the tender are the following: After deciding whether the tender in question contains no legal gaps or mistakes, then, based on a list provided by various social bodies and organizations, we appoint persons in charge of various topics, probably usually two people per topic. They usually prepare their opinion in an open way. Of course later on we will probably keep those opinions secret but for the time being we will keep the tender and the

opinions public to avoid friendly contacts. All blocks of topics have senior officers, like one for the whole field of biotechnology or technical innovations. When the people in charge come up with their surveys, their opinions, then at the ministry we coordinate preferences to tenders accepted. That is, what is the priority in the field. After the decision has been brought, we conclude agreements which contain as one fundamental point that the results will be monitored regularly and if they are not satisfactory, the agreement will be annulled and the institution in question will get no money whatsoever. So it is a tough game. When results are already visible, we want to attract the producer itself as a sort of co-sponsor, sponsoring whole subsidies. In addition to that, we want to increase efficiency to a considerable extent.

George Vojta

Executive Vice President
Bankers Trust Corporation

I venture to offer this message because for 30 years I have been involved as an international banker in every major economic region in the world. Any banker with the experience over this period of time has been involved in the development of the principal Asian economies -- Japan, South Korea, Taiwan, Malaysia, Singapore, Indonesia, Thailand, Hong Kong, and Australia, which today are models for successful development, as well as with those Asian economies which have experienced slow growth or decline -- Vietnam, Cambodia, India, Pakistan, Bangladesh, and Sri Lanka. This involvement extended to Western Europe and participation in the creation of continuing economic prosperity in Britain, France, Germany, Italy, the Benelux countries, Scandinavia, Switzerland, and more recently Spain and Portugal, to involvement in the erosion of the economies of Greece, Eastern Europe, and the Soviet Union in the 1980s, the tragic post-colonial decline in the economies of North and Southern Africa; to the absence, except for Chile, of economic development in Latin America in the 80s, following a period of growth in the 1960s and 1970s, to the dramatic expansion in the U.S. economy in the decade of the 80s, which included the creation of over 20 million jobs following a period of debilitating stagflation in the 70s, to the emergence of prosperity in the oil producing countries in the Middle East and Turkey, co-existing with lagging development in the less fortunate countries in the region, Egypt, Syria, Lebanon, Jordan and Iraq, Yemen, and Afghanistan, and finally to the inconclusive struggle in the People's Republic of China to sustain a course which promoted economic expansion.

This global experience is rich in insight as to what succeeds and what does not succeed in putting an economy on a path of self-sustained growth. The conclusions I wish to submit to you are matters of fact, not ideology. We are beyond the age of economic ideology in the world. Global experience tells us how to develop an economy in very practical terms.

In one sense, all economies are the same. Every economy in the world needs political, fiscal, and monetary stability to achieve growth. All economies have laws, regulations, and a judicial system that govern the conduct of economic activity. Every economy is a mixed economy, part state owned, part privately owned; in every economy, in some sectors, prices, interest rates, and exchange rates are regulated and controlled, in other sectors the market establishes prices, interest rates, and exchange rates. All economies have "underground or informal economies" which accommodate exchanges of goods and services outside the "official" sector of the economy. All economies use controls and subsidies and free markets to varying degrees to regulate economic activity and to allocate resources. Finally, the performance of any economy depends ultimately on the quantity and quality of its human capital, not its natural or financial resources, and how human capital is incentivized and permitted to function.

The differences in economic performance between countries relates to how relatively dominant each of these patterns is in the total economy. An economy that is dominated by state owned enterprises, centrally planned prices, interest rates, and exchange rates, which restricts private ownership and permits market mechanisms to operate only in a relatively small private sector and the "informal economy" will perform differently from economies dominated by private ownership, and market-determined prices, interest rates and exchange rates. In economies dominated by extreme political, fiscal, and monetary instability we find that a large proportion of total economic activity is in the "informal economy". As a result still another performance pattern occurs.

The question before us is: what does the world's development experience tell us about the preconditions for successful economic development and what is the role of Parliament in creating and sustaining these preconditions? There are ten essential preconditions.

First -- Political Stability

Every country that has enjoyed a prolonged period of economic growth in the post World War II period has recorded such gains steadily over periods ranging from about 10 to 20 years, in some cases even longer. Every such country has experienced political stability during those periods of expansion. By political stability I mean that a political coalition which was committed to supporting a specific economic growth strategy held power during that growth period and more importantly used political power to maintain and support the growth strategy of the country. The types of government varied -- some involved one political party which dominated government for a long period (Britain, Japan, Malaysia, Singapore, and Taiwan are examples); or there were a series of governments involving more than one party which shared and supported in the main the same economic strategy (the former West Germany and Australia are cases in point). Some governments were military or dominated by the military (South Korea, Thailand, Indonesia, Chile); some were royal governments (Saudi Arabia, Kuwait); a few were colonial governments (Hong Kong).

In all of those cases, political stability created an orderly, stable environment in which significant savings and investment occurred, establishing a pattern of sustained growth. In contrast, we have seen in country after country that chronic political instability ruins the possibilities for growth.

Second - Law, Regulation and the Courts

In successful countries the ruling political coalition was able to establish -- in stages - a system of law, regulation, and legal process which supported and promoted economic development and to administer that system relatively fairly and efficiently. This framework enabled economic agents to have confidence in the rules governing their activity and in the reliability of "contracts" executed in the marketplace. No economy can grow without such a framework. Growth cannot be sustained in an arbitrary legal and regulatory environment. It is not surprising that the most impoverished countries, that have been unable to grow, are characterized by an absence of such a framework.

Third - Ethical Climate

An ethical climate in which to conduct economic activities is another pre-condition for growth. Every country, my own included, is negatively influenced by graft and corruption. Regrettably this seems to be an aspect of the human condition and realistically we cannot free ourselves totally from it. But in all successful countries graft and corruption were not permitted to become a norm for economic behavior, people and institutions could manage their affairs without having to resort to such practices and not lose the chance to function and succeed. Graft ridden environments drive economic agents away, and the countries involved lose the chance of growth. The correlation between extensive graft and general poverty and economic decline is a clear message from our experience in the post-war period.

Fourth - The Character of Government Regulation

In successful economies, government and particularly the central government, did not monopolize economic decision-making. The character of government regulation permitted the institutional and individual players in the economy significant autonomy to make the decisions about what to do, how to do it, what risks to take and what risks to avoid on the basis of economic considerations only. Regulation of this type decentralizes economic decision making to a considerable degree and has the effect of unleashing the creativity and innovation of the economic agents in the economy. Over-regulation chokes such creativity off and destroys the wealth-creating capacity of institutions and the people. Countries which stagnate or decline are characterized by excessive regulation. In these environments the people are diverted from wealth creating activities and must devote their energies to "win approval" from government for everything they wish to do. Many cease trying or choose to conduct their activities in the "underground economy". The result is loss of productivity and a deterioration in growth.

Fifth - Fiscal & Monetary Stability

A consistent profile of fiscal and monetary discipline to keep prices, interest rates, and exchange rates reasonably stable is another distinguishing feature of successful economies. Fiscal deficits in excess of 4% of GDP, financed by money creation can push economies into dangerous directions. In economies characterized by controlled prices, excessive monetary creation diverts the supply of goods and services into the underground economy and results in a liquidity overhang in the official sector. In such circumstances chronic scarcities of goods and services in the domestic economy and a diversion of exportable goods to illicit channels result, over time the underground economy captures more and more of the total economic activity. This has been your experience in Eastern Europe.

In economies in which the markets determine domestic prices, exchange rates, and interest rates, excess monetary creation runs the risk of driving the economy to high or hyperinflation. The growth process can be destroyed when domestic inflation moves beyond 20% per annum for protracted periods. The hyperinflation in some of the Latin American countries today is a vivid current example. Hyperinflation drives all economic activity into the informal economy, encourages capital flight, flight from the domestic currency, a recourse to barter transactions, and above all, a decline in economic growth.

Sixth - Rates of Domestic Taxation

Economic growth involves creation of wealth by institutions and individuals functioning in the marketplace. People and economic institutions innately want to better themselves, they want to create wealth and retain a meaningful portion of the wealth they have created. Countries which have become prosperous have set tax rates at levels that permit this to happen. They have collected such taxes as were levied fairly and efficiently to keep the finances of the state on a sound basis, but allowed institutions and individuals to retain a sufficient percentage of the wealth they created to give them incentive to continue efforts to create more wealth; this dynamic keeps overall growth moving forward. If taxes are too high - as they were in a prosperous country such as Sweden in the 1970s, institutions and people try to avoid paying them by diverting their activities to the underground economy - or worse they stop trying to create wealth because they do not receive an acceptable return; again overall growth in the economy declines. Every successful growth economy has held a tax policy that motivated institutions and people to continue the process of creating wealth.

Seventh - Market Mechanisms

Increasingly predominant, but not necessarily exclusive use of the market to allocate resources, establish domestic prices, interest rates, and exchange rates characterizes those economies that have had the best growth rates in the last 45 years. The record shows that markets, though not free of problems and malfunctions, allocate total

resources in the economy more efficiently than alternative mechanisms. In today's global economy, this is more true than ever. The experience is that non-market prices divert goods and services from the official channels of the economy; non-market interest rates do the same for money; non-market exchange rates divert foreign currency to black markets, suppress official exports and imports and create inefficient producers of goods and services that cannot compete in world markets - a formula for disaster in the long run. No country in the world relies totally on free markets to allocate resources. There are strategic national industries to be protected. OECD countries and Japan all subsidize their agriculture, their defense industries, their computer industries, etc. But in the main, progressive economic development and progressive global competitions have come as a result of a progressive shift in favor of market mechanisms to allocate resources and establish prices and rates.

Eighth - Private Ownership

Principal reliance on the private sector to create wealth (with the support of the state) has been another indispensable strategy to promote economic growth. The universal experience with state-owned enterprises in the past 45 years is that they are inefficient, uncompetitive, and in the end require the society at large to bear enormous losses to the detriment of all. There are some exceptions (state-owned entities permitted to operate free of arbitrary political control), but the general pattern is overwhelming. The private sector operating in a favorable climate and properly incentivized has been the wealth creating agent that led countries forward. Recent experience in countries such as Turkey, Spain, and Chile are visible examples of how prosperity develops as the economy is privatized. A properly incentivized private sector can create wealth irrespective of whether the country has natural resources or not, is financially strong or not. For example, Japan, South Korea, and Singapore did this beginning in the 1960s and when the process started, these three countries had few natural resources and were financially weak. The private sector created and attracted the resources needed to create wealth in the economy.

Ninth - Liberalized Markets

A progressively liberalized external sector of the economy which maintained competitive exchange rates, a convertible currency, reduced import tariffs and quotas, and encouraged foreign investment, and the importation of technology and skill characterizes successful economies. The results of these policies are significant growth and diversification of exports (South Korea, Chile are obvious examples), globally competitive domestic enterprises, sufficient capital, technology and skill to maintain high levels of productive investment and a viable balance of payments position throughout the growth process. Restrictive external policies suppress exports and imports, create inefficient domestic enterprises, and cause a scarcity of capital, technology and skill, and balance of payments crises, all adverse to an economy's development.

Tenth - Human Resources

Human capital is the decisive resource in achieving economic growth. Skilled people, working in the marketplace, incentivized to create wealth, overcame every problem or barrier to economic growth in the successful countries. All successful countries made continuing investments in their people and saw to it that they were rewarded during high growth periods for successful economic activities.

All too briefly, this has been the set of preconditions that were present in countries which have had the greatest success in growth and development in the post World War II period. This is the profile which attracts the support and interest of the world community. It is the profile which is supported as the model for growth by the World Bank, the International Monetary Fund, the regional development banks, the Export-Import Banks and domestic and foreign investors. It is the model which attracts the necessary resources in sufficient quantity and quality to support growth. It is the model which the entire economic experience of the post war period confirms over and over again as the best model, and fortunately, it is the model that many countries in Central and Eastern Europe have embarked upon or are considering. I recognize that for many of you this model is not without difficulty or controversy.

As you know very well, this model differs greatly from the economic profile of your countries in recent years. Your economies have been dominated by state ownership, by strong central regulation and control of economic decisions, by non-market prices, interest rates and exchange rates, by a relatively small role for private enterprise and a restrictive external policy. Given the world-wide experience in development, it is not surprising that the performance of your economies has not been satisfactory to your people and very appropriately, you have concluded that a new direction is necessary. But you have concerns.

Movement toward the model that has succeeded best in creating economic growth requires a different perspective on a vital issue. Many of you are concerned that such a model for the economy will result in great disparities of wealth in your societies -- and that to some of you is objectionable. It is true that economies of this nature create disparities in wealth while also creating prosperity for everybody. But let me point out that in your economies with so much economic activity flowing into the informal or underground economies over the past several years, the disparities in wealth that have resulted are extreme. In addition, society as a whole has not enjoyed prosperity. Changing the direction of your economy toward the model that works gives all of your citizens an opportunity to make their lives better, and they will. Over time you will create more wealth for everybody. Disparity of wealth is present in your economies today; in your future economies disparity of wealth will remain but all will prosper. Secondly, many of you are concerned about the processes of adjustment to the new economy, in particular the cost in terms of short-term unemployment. These costs are real but this dislocation can be overcome in a reasonable period of time by the important job creation arising from the formation of new small businesses; already in

Hungary, Poland, Czechoslovakia this is occurring. The experience around the world is that new and small businesses create most of the new jobs in the economy. This was certainly true in the United States in the 1980s; almost all of the over 20 million new jobs were created by small and new businesses. You can have confidence that there will be enough jobs if you pursue these workable, general strategies and continue to permit small businesses to be established and grow.

In the context of the foregoing, what is the role of Parliament in the process of launching and keeping your countries on the proven path to growth? In a phrase -- Parliament's role is **indispensable**. Parliament must maintain the critical political consensus which supports the growth strategy, and provide political stability, constancy of leadership, and use of power to promote economic growth. Parliament must pass the laws, oversee the regulations, and the courts to create and maintain the legal framework which supports growth. Parliament must be the moral standard for the ethical climate needed to conduct economic activity properly. Parliament must insist on a standard of regulation that permits institutions and individuals the freedom to pursue the legitimate creation of wealth. Parliament must pass budgets that keep the country fiscally sound and oversee the conduct of fiscal and monetary policies to prevent excessive and destructive money creation. Parliament must create a tax climate that sets and collects appropriate taxes efficiently but assures that tax policy permits people and institutions which create wealth to retain suitable portions so they are motivated to continue to create wealth for the society. Parliament must insist on the power that achieves market-oriented price, interest and exchange rate policies, liberalization of the external sector, and significant privatization of the economy. And finally, Parliament must direct social investments and policy initiatives that maximize the quantity and quality of human capital -- the capital upon which economic growth depends.

Parliament represents the people, the people want to prosper. They are willing to try -- given the chance -- to make life better for everyone. Distinguished parliamentarians, you have great responsibilities and an historic opportunity to make life for your countrymen better forever. You will succeed and success will come faster than you think. I wish that I was one of you.

Charles Taylor

Executive Director, Group of Thirty

Consultative Group on International Economic and Monetary Affairs, Inc.

It is an honor to co-chair this session before such a distinguished gathering of parliamentarians from Eastern and Central Europe, the United States and the German Federal Republic.

I speak to you in my personal capacity. I am the executive director of the Group of Thirty. This is a small group of bankers, central bankers and economists from around the world who share a common concern for matters of international economic and financial policy.

We, who have been observing the changes underway in Eastern and Central Europe, are in awe of how much has been achieved in the last few years. We congratulate you. But we note, also, that a great deal remains to be done.

Speaking from the perspective of those who might consider investments in your region, I thought it might be useful to discuss some of the policies that may help attract foreign capital and stimulate trade with the West.

First, on trade: Your basic strategy is clear. Full convertibility and limited use of tariffs. I noticed in Minister Kádár's remarks this morning that average Hungarian tariffs have declined from 30% to 16% in the past short while. The process is already underway.

I would add, you do not need export incentives; nor do you need import controls; simply keep the exchange rate competitive.

So far as imports are concerned, I would stress one temptation that is to be avoided: do not attract foreign direct investment by providing any type of guarantee of protection from imports. It was fashionable at one time to encourage investments with the promise of exclusive rights to a domestic market. We now know that the costs of encouraging investment this way are generally unacceptable.

There are two things we in the West can do: help finance your trade and open our markets.

(I) Help establish your own export credit agencies. There is no reason why your exporters should lose orders to Western competitors purely because they do not have the same kind of hard currency financing available.

There is a good case for the industrial countries instructing one of the multilateral agencies, such as the European Bank for Reconstruction and Development or the European Investment Bank, to reinsure guarantees from your export credit agencies. Why? To encourage Western banks to put up the necessary hard currency on regular terms.

This is a proposal contained in the forthcoming Group of Thirty Report on the Financing of Eastern Europe. I understand that it has been well received in some quarters here. There is a chance that the United States will sponsor the idea at the summer summit, but it must have wholehearted support at the highest levels, including parliamentary support, in East and Central Europe if it is to come about.

(II) We can also help by opening our markets. I note again that Minister Kadar referred to Hungary's participation in the GATT and its seeking association status with the European Community. I strongly endorse such initiatives.

It is imperative that the industrial countries open their markets not only to your industrial exports, but also to your agricultural exports as soon, and as completely, as possible.

On investment, I have four points:

(1) Set up a uniform regime for foreign direct investment; do not negotiate deals here and there, giving special tax holidays and other particular incentives. By and large these things do not matter to investors. They take them if offered, but they rarely make them do an investment they would not otherwise do. And they distort the pattern of investment and hurt public finances.

(II) Full Convertibility: In particular, allow the full repatriation of profits. If you set up the right kind of investment climate, businessmen will not want to repatriate profits. If you force them to keep profits in your countries, they will find ways around it and take it as a sign that you are not serious about fully joining the world trading and financial system.

(III) Grant exemption from historic liabilities: for example, you may reasonably require a foreign investor to use a clean technology to produce, say aluminum, but make it clear that he will not be held liable for cleaning up pollution by the enterprise, before he bought into it. If there is no guarantee on this score, it will be very difficult to get as much participation of foreign capital in your privatization programs as possible.

(IV) Maintain the direction of reforms: if you chose an aggressively liberal economic system like ours in the United States, all well and good. If you choose a social market economic model, like Germany's, also this is quite acceptable. But, my advice would be, it is important from the perspective of foreign investors that you stick to it. If three years from now, say, it seems to businessmen and financiers in the West that your basic commitment is wavering, then all the good work of the previous three years will be lost--so far as they are concerned.

This brings me to my last point. Reforms will have to be comprehensive, and well established, before most of your countries can expect any large private capital inflows. Your main source of Western financial support for the next five years will be official assistance. Then, or soon after, official flows are likely to taper off. It is important that, when they do, your economic transformations are very well advanced. As Speaker Szabad noted in his opening remarks, the role of parliamentary oversight will soon become crucial. For it is not enough to pass laws. They must also be implemented in

both the letter and the spirit. Then, private capital inflows will begin to become significant.

I am confident that you can maintain the momentum toward fully market-based economic systems. I am confident that a good deal of investment will eventually come from the West and will be a valuable catalyst to your efforts. I look forward in anticipation to that day.

Charles Vanik
Squire, Sanders & Dempsey
Former Member, U.S. House of Representatives

Parliamentarians in America

As a retired, American former parliamentarian, without hope, desire or expectation of a reincarnated parliamentary life, perhaps I can speak with more candor.

Parliamentarians are essential to government since they are the connecting link between people and their government. They legislate or more specifically approve or ratify policy which they can create or generate. More often they choose to approve or disapprove a policy submitted by an executive.

Contrary to popular assumptions, parliamentarians are not likely to create chaos or policies of legislative disaster -- they merely approve a policy or proposal submitted by others, usually by the executive branch.

Parliamentarians have the power to create policy by developing a plan and promoting it successfully to adoption. However, the longevity of parliamentary service is threatened by those who take their place at the front or the head of change and seek to "propose" as well as "dispose". Only occasionally and rarely, do successful parliamentarians choose to take a place at the front of change. Their skill is to determine when to place themselves in the forefront of change and lead it before they are overtaken. They are skilled in determining how to test the waters of public opinion so that they can lead without being too early or too late. They become expert at "timing". Those who miss timing success are not likely survivors.

Through experience, a well trained parliamentarian can have a much longer tenure than the regulated terms of the executive, the President or the Prime Minister. In America, there are discussions under way to limit the number of terms or years a parliamentarian may serve.

I believe that term limitation in America would not be in the public interest. Compulsory rotation would eliminate career parliamentarians and would result in a lower quality of candidates who would pass in and out of legislative work through a revolving door using legislative work as a stepping stone to some other career instead of a career goal in itself. Temporary passions of the people would become the law of the land. Expediency of the day would supercede long-term policies carefully deliberated. It is the senior, experienced parliamentarians who can uniquely link and adjust change with a historical perspective and by preparing for change on a gradual basis rather than abruptly. Parliamentarians must be committed to living with legislative decisions and being responsible for their consequences. The short-term parliamentarian escapes responsibility for acts of legislative oversight or folly.

Many parliamentarians complain about the frequency of elections. However, frequent public elections provide more effective public review. The parliamentarian is always concerned about the next election -- and that's how it should be.

One of the unadvertised reasons for long-term incumbency of the U.S. Congress results from the congressman's efforts as an ombudsman -- in providing special services to the constituents by urging the bureaucracy to respond to citizens requests. There were times when my constituents disagreed with my voting record and continued to provide me election support because I served their many non-legislative requests. Constituent services as an expeditor of constituent needs permitted me to survive at times when my voting record was at variance with constituent demands.

My counsel to parliamentarians is to learn the art of survival -- the art of moving policy as well as it can be moved, without facing certain defeat. Winners make decisions. However, in the life of every parliamentarian there is a cause more important than all things -- on which he must risk his tenure and his future. The parliamentarian must be prepared to take this risk when he is commanded by his judgment and his experience. Parliamentarians are expendable and replaceable and the good parliamentarian must with grace choose between principle and tenure.

The Jackson-Vanik Amendment

In the last part of the decade of the 1970s, I gave a good part of my efforts in the implementation of the now ancient "Tokyo Round of Negotiations" [under the GATT].

Many U.S. businessmen consider the part which the late Senator Jackson and I had in the Trade Act of 1974 as a trade obstacle because it restricted trade between the U.S. and non-market economies unless they recognized the "rights of their citizens to emigrate." This amendment of course restrained and reduced U.S. sales to non-market economies to the advantage of our trade competitors in other countries. No other nation adopted such a law and I was disappointed. Many of our trading partners used our laws to facilitate the repatriation of their own ethnic groups.

However, the Jackson-Vanik Amendment served notice to the world that the course of human rights was more important than profits for commerce. The Helsinki accords internationalized the idea without providing an enforcement tool.

In America, the Jackson-Vanik Amendment occurred in part as a reaction to the shock of the U.S. Congress sustained on discovery of the huge commitment to the Vietnam War. The Amendment was an effort of the U.S. Congress to reclaim its jurisdiction in international trade matters. The Amendment was a forerunner to the War Powers Act and a tremendous array of changes to bring congressional power into alignment with responsibility to the electorate.

For better or for worse, the Jackson-Vanik Amendment moved the U.S. Congress into the trade deliberation process which prior to 1974 was the exclusive domain of the executive.

The U.S. Congress is not likely to relinquish its involvement in trade. Nor is the Congress likely to strike down the amendment. This law will remain in the code -- available for use again if world conditions change. Other parliaments are different. Their parliamentarians serve in the executive role when the political party is in power. Under these circumstances, they share executive decision power.

I want to take advantage of this moment to discuss a related trade subject. Under present U.S. laws, American participants in international trade are prohibited from offering inducements of personal value to those who have the power of contract decision on behalf of their principals.

A few American businessmen believe that a repenting U.S. Congress will change its mind on this issue. In my judgment, this will not happen. The American Congress is not likely to change or repeal these rules.

Although there are places in this world where trade cannot exist or flourish without these inducements, Americans are rightfully in fear of the consequences and often decide against competing in places and countries where personal inducements to trade are an accepted practice. I find no comparable contract integrity restraints in trade laws of western Europe or the European Common Market.

As the eastern European democracies move toward market economies and economic freedom, it would appear to be on the side of wisdom to pass statutes or make declarations directed toward international trade integrity. Products and services brought into world markets must be of good quality, low price, promptly delivered and efficiently serviced. Goods and services that enter markets as the result of private inducements to the contracting parties cannot meet this test. It is the consumer who suffers when the product or services offered must include the pernicious cost of private contract inducements.

World trade must flow freely -- without private inducements to the contracting parties. It is my hope that the new democracies and their parliaments will insist on some form of trade integrity.

Vera Trojan

Assistant Vice President
Wellington Management Company

Many of the parliamentarians speaking at this conference have noted that foreign capital can play an important role in economic development, and in the process of marketization and privatization. It can bring with it technological and managerial expertise, and access to Western markets. Foreign capital, in short, is something all of the countries represented here want to attract.

At the same time, the global situation is a difficult one. The world is faced with enormous capital demands from all corners of the earth: your own, Africa, China, Latin America, the United States, even Germany and Kuwait. In the face of this discouraging environment, it is important to remember that each year a tremendous amount of money does flow across the borders, searching for the world's best investment opportunities. In 1989, for example, private sector capital flows from the United States, including foreign direct investment (\$32 billion), portfolio investment (\$22 billion) and bank lending (\$51 billion), totalled \$103 billion.

The share of Central and Eastern Europe of this total has been very small, despite a tremendous amount of interest. Many investment funds have been set up in the financial centers of New York, London and Tokyo for the express purpose of investing in Central and Eastern Europe. To date, the money that these funds have raised remains largely uninvested. Many corporations are interested in investing in your countries. While the flow of foreign direct investment has increased, it is small in comparison to your investment goals.

The cruel reality is that investors do not give their money to those who need it most. We often joke that the easiest way to get a bank loan is not to need one. Investors are looking for return, which can take the form of income flows or capital appreciation. They are looking to commit their money into a situation, which through growth, increased efficiency or innovation, will increase the value of their commitment.

Western investment is allocated according to a straightforward risk/reward framework. Very simply, investors are willing to take on incremental risk only if it brings with it a commensurate increase in return. Managers of portfolios of stocks and bonds, such as myself, seek to maximize the expected return per unit of risk, often as measured by the historical volatility of an investment opportunity. Direct investors apply the same concept in determining the interest rate at which they discount the

potential returns from a new investment. Banks reflect this concept in the spread over a risk-free rate they charge on loans to different borrowers.

My most important message to you today is that you can do a great deal to improve the risk/return tradeoff of investing in your countries. Once you understand the sources of risk, as perceived by Western investors, you can often take straightforward steps to alleviate them. You can also influence prospective investment returns. And you are now competing for investment funds with other countries who are doing just that.

Risk, in the eyes of Western investors, comes from political or economic instability, a lack of stable laws and Western standards of compliance. It comes from a perception that rules of the game will be changed or applied arbitrarily. Risk often comes from our own ignorance: lack of knowledge about local business partners, practices and opportunities. It is caused by lack of disclosure: a poor accounting system or a price system that does not reflect market value. Risk stems from perceptions of the work ethic and attitudes of the local labor force. Risk implies that you might make a poor return on your investment, or not be able to take your money out.

Expected returns are higher if you offer good value, whether in your labor force, resources or expertise. They seem more assured if others have been successful in your country, or if you offer good management. They can be influenced, in one direction or another, by taxes, liquidity and the monetary regime.

Of course, Western investors and businessmen are used to taking on risk. It can never be eliminated completely. But let me quote here a prominent American investor, who was recently interviewed by The New York Times:

"I don't need to go half way around the world to lose \$2 million," he said. "I can do it right here at home."

There are many things that parliaments can do to improve the risk/reward tradeoff of investing in their countries. Many of these are outlined in the CSCE Bonn Document on Economic Cooperation in Europe. The primary goal is to create a framework that allows investment to take place, and assures investors that their rewards will be protected. Specifically, I would like to highlight the following:

1. Establish a stable and predictable legal framework, including laws governing ownership and government/corporate disputes. Create a mechanism that allows private contracts to take place.
2. Establish a tax code that is predictable and inflexible.
3. Support your legal and tax codes with Western standards of compliance. Avoid arbitrary changes and exceptions.

4. Cherish your investors -- both foreign and local. The best evidence of the potential of your country is that your own people are making money. If your own businessmen are successful, foreign capital will follow. But do not protect your businesses from competition.
5. Parliament also has an important role to play in presenting its country to the world. Conferences such as this one play an important role. Know where your strengths lie, what you have to offer, and which industries you want to grow. Tell the world about the benefits of investing in your country, and do it over and over and over again.
6. Parliaments can play an important role in promoting liquidity and disclosure. Investors want to be assured they can take their money out, or move from one investment to another within your country. Work toward creation of secondary markets, a market price system and currency convertibility. Remember that capital controls are often a recipe for capital flight. Information also promotes liquidity. It takes on a critical role when foreigners enter a country they do not know. In their own countries, they do business with firms they know in a system that is understood. In a new environment, even more emphasis is put on disclosure, a good accounting system and an understanding of costs and subsidies. Provide the information on a regular and consistent basis.
7. Finally, and perhaps the most importantly, get out of the way. Your most valuable role is to create the standards, mechanisms and stability that inspire investor confidence. Then give individuals the flexibility to shape their own commerce.

John Williamson

Senior Fellow

Institute for International Economics

One of the advantages of initiating a program of comprehensive economic reform at this particular date in history is that there are certain misleading pieces of economic advice that might have been given by economists in the past but which are unlikely to be dispensed today. For example, 20 or 30 years ago, there would have been many voices advising that the route to development lay through import-substituting industrialization and the avoidance of foreign investment. Nowadays virtually all economists would agree that such advice is unwarranted, and would recognize the advantages of outward orientation. Since we are in Budapest, let me mention that one of the leaders of this revolution in attitudes was a Hungarian by birth and upbringing, namely, Bela Balassa, whom I am privileged to count as a former colleague at the Institute for International Economics and co-author of a paper on balance of payments policy in East Asia.

Outward orientation enables the foreign sector to play three key roles in promoting growth:

1. It allows growth to be export-led, thus ensuring that it will not be interrupted by repeated balance of payments crises.
2. It permits technological modernization via the importation of advanced capital goods and the establishment of foreign direct investment.
3. It creates competitive pressures from abroad in the tradable goods industries, thus leading to a structure of relative prices that reflects scarcity and so too allocative efficiency.

Outward orientation requires four types of policy.

1. A Liberal Trade Regime

Any quantitative restrictions on trade should be replaced by tariffs at a very early date, preferably at the same time that internal prices are liberalized. Thereafter tariffs should be reduced gradually over a period of several years. The ultimate objective should be a trade regime close to free trade, either with a low uniform tariff (perhaps of around ten percent) or by membership in the projected European Economic Space, which might be accomplished by joining either the EC or EFTA (depending on the options that are offered by the existing members). In the interim, until that stage is reached, many of us would see significant advantages in the countries of East and Central Europe getting together to form a preferential trading area (either a common market or a free trade area) among themselves.

2. Currency Convertibility

Not much would be gained by the government abolishing formal trade restrictions administered by the trade ministry if potential importers were denied the opportunity of buying foreign exchange in order to pay for goods that they wished to import. Hence an essential complement to a liberal trade regime in integrating an economy into the world economy is a convertible currency. The degree of convertibility that is necessary is essentially what is referred to in Eastern Europe as "internal convertibility" (i.e., the right of enterprises to buy foreign exchange when needed to pay for imports of goods or services). In addition, foreign investors need the right to remit profits into their home currency if foreign direct investment is to be encouraged. There is no objection to leaving tourists and households to undertake their transactions, including the export of capital, on a parallel exchange market. If an economy is well-managed, with reasonably tight macro-economic policies, then under normal circumstances the premium on the parallel market will be small. But it is a mistake to liberalize the export of capital in a situation where capital is needed for reconstruction at home and

before an offsetting inflow would be likely to develop; capital account liberalization should wait until reconstruction has been accomplished.

3. A Competitive Exchange Rate

As Charles Taylor emphasized in his remarks, it is crucial that the exchange rate be set at a competitive level, since this is the key to establishing export-led growth. However, the exchange rate should not be devalued more than is necessary to persuade enterprises of the advantages of exporting and investing in new export industries: a hyper-competitive exchange rate will do little extra to stimulate export activity even in the medium term (since enterprises will doubt whether it is likely to persist). Devaluation is stagflationary in the short run; it pulls up prices, and in that way reduces the real value of the money supply and cuts real demand. Hence devaluation should be no greater than is needed to stimulate exports.

There are four reasons why a "fixed" exchange rate should be preferred to a floating exchange rate in an emerging market economy. The first is that it helps to have a fixed exchange rate immediately after a program of stabilization and liberalization so that foreign prices can provide a point of reference for the new price structure that is being imported. The second reason is that an emerging market economy tends to be subject to important shocks, most notably of an increase in the demand for money (of uncertain magnitude) that invariably follows a successful stabilization of prices, and these shocks preclude an informed monetary policy based on control of the monetary aggregates. The third reason is that a floating exchange rate requires well-developed capital markets in order to absorb shocks efficiently. The fourth reason is that even economies that have those advantages, which the emergent market economies do not, have often generated misaligned exchange rates. Hence, I conclude that it is better to peg the exchange rate than to allow it to float. However, given the costs of an overvalued exchange rate, countries should be prepared to devalue promptly if that proves necessary to maintain a competitive exchange rate because of differential inflation.

4. Foreign Direct Investment

It would be a mistake to regard foreign direct investment as the primary engine of growth. It is most unlikely to be available in sufficiently large quantities to play such a role, so that a country which relies on foreign direct investment to drive its modernization may never get the process underway. Nevertheless, foreign direct investment can play a very constructive role in supplementing domestic investment and filling in gaps that would otherwise exist. Hence policy should welcome foreign investment--but on equal terms to domestic investment. Not only should 100 percent foreign investment be allowed and bureaucratic obstacles be swept aside, but convertibility should be extended to allow foreign investors to remit their profits as of right. In addition, investors should be allowed to withdraw capital that was registered with the exchange control authorities when it entered the country.

East European Performance

How does the performance of the countries of Eastern Europe match up to the four policy needs sketched above?

With regard to trade, no one can complain that East European countries have been too timid in liberalizing. On the contrary, some of us worry that the tendency to go very quickly to low tariffs with no regional preferences may constitute a case of overshooting that will lead to too many of the region's enterprises closing down, and thus to an unnecessarily severe recession.

So far as convertibility is concerned, countries--led by Poland and Yugoslavia--decided to move quickly to convertibility. It makes a great deal of sense for East European countries to give convertibility a greater priority than West Europe did during its post-war recovery, because of the need to import competitive pressures and a system of relative prices that reflects scarcity--needs that were not present in West European countries in the same way because Western Europe had a functioning market economy even in the early post-war years. Most Western economists salute the courageous decisions that have been implemented in the region over the past eighteen months.

So far as exchange rate policy is concerned, most countries have chosen to peg their exchange rates, and where that is not the case--as in Bulgaria with its floating rate or in Romania with its new foreign exchange auctions that create a de facto dual exchange rate system--there is a compelling reason for the decisions, arising from the acute shortage of foreign exchange. One of the most important reforms in the Soviet Union was the unification of the exchange market last fall. However, some of us worry that Poland and Czechoslovakia devalued too much at the time of stabilization and thus intensified their recessions more than was necessary. Furthermore, Poland now seems in danger of sticking too long to an exchange rate that is becoming uncompetitive, thus running the risk of repeating the unfortunate events so often witnessed in other countries where the government tries to stop inflation by holding a constant exchange rate and eventually has to give in, forfeiting its credibility in the process. And Bulgaria would seem to be risking an inflationary outburst with its floating exchange rate.

The countries of the region have opened the door to foreign investment and are now making arrangements for allowing foreign investors to remit their profits through the official exchange market, just as recommended above.

While policy towards opening the economy to the outside world in Eastern Europe has not been free of error, the record is a creditable one. One hopes that it will begin to pay off with a resumption of growth, leading ultimately toward catch-up with the West, before very long.

Marie Lavigne
Professor, University of Paris Sorbonne
Director, European Studies Center at Stirling

I want to address an issue which has several times briefly been mentioned here,¹ i.e. the need for a specific regional arrangement for trade and economic cooperation, including cooperation in the field of investment, in East Central Europe.² I would like to recall where we stand now, and suggest some possible solutions.

I. Where do we stand now?

We have heard here that the regional trade was collapsing. Indeed, trade among the European CMEA (Council for Mutual Economic Assistance) members has declined by 20 percent in 1990, and a further decline of perhaps 30 percent in 1991. Presently the situation is explained by the Soviet economic and financial crisis. The U.S.S.R., it is said, cannot any longer supply its partners with the oil and gas they need and got previously. Due to a lack of hard currency, it has to cancel a large share of its import contracts from Eastern Europe. These trends are true. To insist on these reasons ignores the fact that trade among Eastern European countries (the U.S.S.R. excluded) has also dropped. Even if the situation of the U.S.S.R. had not so dramatically deteriorated, the logic of the "reform" of the CMEA rules would have brought about the present stalemate.

Actually the intra-regional trade is not regulated any more. It would be deeply misleading to believe that trade in hard currency and at world prices has replaced, since January 1991, the former arrangements for trade in transferrable rubles and at specific prices. The old system has disappeared. The traditional intergovernment bilateral trade agreements are now void. But the new rules are not applied because not a single country is yet prepared to spend its precious, painfully earned dollars and DM on purchases from its former CMEA partners. What is true on the macro level is also true on the micro level: the Eastern enterprises now prefer to purchase in the West what they used to buy--rather, to get, along arrangements imposed on them--from their neighbours, even if they have to pay more. The result is that apart from a minimal,

¹ In particular by Minister Béla Kádár, Harald Malmgren and John Williamson.

² I speak here as an independent scholar; I am currently on leave from the University of Paris Sorbonne, and Director of the European Studies Center in Prague which is a branch of the Institute for East-West Security Studies in New York. I do not express the views of the IEWSS European Studies Center; the Center itself is however, concerned with this issue, and among its practical assistance activities has set up a study group on the question of intra-regional trade, to which it has devoted a conference in November 1990.

basic trade, often still regulated by bilateral clearing now denominated in hard currencies, the previous flows are collapsing all over the region. Simultaneously, protectionist barriers are growing among the CMEA members just when the same countries dismantle their protection mechanisms as regards their Western partners. This is true in particular for non-commercial movements: tourist flows are now constrained because no country accepts to be "plundered" by its neighbor's citizens, and all over the region, with a few exceptions,³ hard currency is required to travel in the East as well as to the West. Coupled with the exchange controls on private movements, the unconvertibility of the domestic currencies of Eastern European countries among themselves strongly limits tourism and generates practices of illegal arbitrating on these currencies. As for commercial flows, they are increasingly handled by Western compensation houses which gain in fees the benefits of the "vacuum" now existing in the regional trade.

This situation is not only an additional burden on the transition but may also provide an argument against increased assistance: should one help each individual country when the region as a whole is collapsing?

II. What might be done?

I am pleading for a new arrangement in Eastern Europe, facilitating among others trade and investment. Such an agreement should obviously comprise some provisions for settlements, but I shall not discuss here the plans for a new East European Payments Union, first because we are focusing here on trade and investment, second because it seems to me that this issue has been too much emphasized (in a positive or negative way) compared to real issues (see for instance Kenen, 1990, van Brabant, 1990).

As such proposals are very unpopular now in Eastern Europe, I want immediately to state that I do not suggest to revive the former CMEA in its political or economic dimensions. Such a scheme is not meant either to keep these countries from integrating within the EEC; with or without it the integration is going to be a long process. Unfortunately, the new organization which is to replace the CMEA is not going to help much. This "Organization for International Economic Cooperation" which might be created next month, in April 1991, bears little resemblance to the OEEC (Organization for European Economic Cooperation) which was created after the war (1948) in the wake of the Marshall Plan and was so successful not only in coordinating the Marshall aid (on the basis of the European Cooperation Act imposed on Europe by

³ In particular between Czechoslovakia and Hungary, as we have been told during the Conference.

the donor country, the USA) but also in preparing the ground for the future Common Market.⁴

A new regional arrangement might address the following issues:

- Trade: if free trade cannot be introduced without delay, then some agenda should be set up to this effect;
- Cooperation in legislation (here the role of the parliaments would be crucial) in many fields: the drafting of company laws according to the same model which might be the new European Company; legislation on foreign direct investment, to stop a damaging competition among the countries struggling to attract such investments; anti-trust and anti-monopoly legislation, to mention a particularly critical issue in Eastern Europe; legislation on environment; etc.

Should such an arrangement include the U.S.S.R.? The present developments are basically against it. The Visegrad Summit, in February 1991, establishes cooperation between Poland, Hungary and the C.S.F.R., the "hard core" group of the transition to the market, and the Final Declaration recommends "free movement of capital and labor", to be promoted by "the development of market-based economic cooperation", cooperation in infrastructure development, in the ecological sphere. But no explicit mechanism or regulations are to ensure that the goal be met.⁵ Could the U.S.S.R. be part of such an arrangement? Obviously it should, as it is the main problem for trade. But its participation would also create political problems, and in addition one does not know what the U.S.S.R. is to look like in the near future. For this last reason, one should begin with a limited number of countries--the important thing is to begin.

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⁴ I am very grateful to Mr. Raymond Barre, former French Prime Minister, and who worked after the war three years with the OEEC, for having pointed this out to me.

⁵ Text of the Visegrad Summit Declaration, Report on Eastern Europe, Radio Free Europe/RL Research Institute, March 1, 1991, p. 31-32.

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A Short Summary on Economic Development Through Economic Integration and External Policies

1. Elimination of Trade Barriers

A. Basic Premises

-- To make transition from self-sufficiency-oriented planned economy to a competition-oriented market economy based on achieving competitive superiority.

B. Gradual Increase in the Approval for Merchandise Imports

-- To move from the positive system to a negative system, and ultimately achieve total market liberalization.

C. Gradual Elimination of Tariff Barriers

-- Gradual decrease in tariff rates.

-- Decreasing other miscellaneous fees and taxes, to eventually abolish all tariff barriers.

D. Abolition of Non-Tariff Barriers

- Restrictions on foreign currency remittance.
- Control of foreign exchange rates.
- Import and export quotas on certain goods.
- Legislation on "Buy Local" programs, to induce purchasing local goods.
- Government subsidies to local producers.

2. Inducements for Foreign Capital and Technologies to Create an Environment for Investment

A. Basic Premises

-- To make transition from isolation to liberalization, on inducing foreign capital and technologies to local industries.

B. Guarantees on Investments

- Legal systems for establishing a company: a joint management regulation.
- To guarantee foreign remittance of capital profit.
- To guarantee foreign remittance of paid-in capital, in case of corporate withdrawal.
- To guarantee external payments of technological fees and commissions.

C. Guarantees on Company Operations

- Full autonomy on pricing decisions.
- Relieving problems of inconsistency between corporate goals and national policies, in cases of exports.
- Making possible foreign currency exchange of domestic revenues for overseas remittance, in cases of domestic sales.
- Freedom to import or procure from domestic sources the necessary parts, raw materials, and components.

- Allowing the foreign management and technicians to enter and stay within the country.

- Free employment of labor; recruiting labor and termination of employment based on market principles.

D. Providing Incentives for Investments

- Tax exemptions for a specific period of time.

- Income tax breaks on corporate income and personal remunerations.

- Priority on allocations of necessary foreign funds and capital.

- To guarantee registration and usage of patents and trademarks.

E. Methodology

- A step-by-step approach to market liberalization: expanding Free Economy Zones.

- To make further liberalization, from present restrictions on allowing only joint ventures to allowing even 100 percent wholly-owned foreign entities.

- To allow other forms of investments from direct investments to even indirect investments, as the securities market is established.

3. Corporate Role in Economic Reforms

A. A Mixed Economy

- Co-existence of public and private sectors within the economy.

- Co-existence of corporate autonomy and government control.

B. Role of the Government

- Controlling the allocation of crucial resources and providing incentives will facilitate corporate development.

- Government policies for registration and approval, regulating market oligopolies, and prohibiting unfair commercial practices, will restrict undesirable and negative activities of the firm.

-- Environmental protection and consumer protection will foster the regulation of corporate activities, for maintaining and facilitating public benefit.

-- In the case of Korea, industrialization strategy has been implemented under government initiative, in order to expand the business infrastructure and create strategic industries.

C. Role of the Private Firm

-- A major role in economic growth, to take on the role as the main body for production and marketing.

-- Maintaining and developing the system of market economy, under the principle of competition and incentives toward making profit.

-- Fostering of innovation.

-- Creating employment opportunities in the labor market.

-- In the case of Korea, private firms have induced foreign capital and technologies, taken on the leading role of developing the economy through exports, trained and educated competent managers and engineers, and formed a strong capital foundation, all under the government's export-oriented industrialization strategy.

VII. PRIVATIZATION

Highlights and Commentary

Private property and individual economic rights are central features of a market economy. Dismantling state-owned monopolies and establishing new forms of ownership require a new legal and administrative framework to guarantee property and ownership rights, as well as mechanisms for stimulating entrepreneurship and creating pools of private capital. Privatization is a central issue of concern, not only because of its importance in establishing the basis for a more efficient and productive economy, but also because, as Michael Silverman observed, it cuts across all spheres of economic and social activity. In developing privatization laws, the Central and Eastern European parliaments must take care to maintain basic policy consistency along all the fundamental dimensions of transformation that come into play. All of the countries in transition consider the diversification of forms of ownership to be a high priority. However, there is no consensus on the best approach to privatization; the basic policy questions underlying privatization efforts are being resolved differently as each government attempts to balance the often conflicting requirements of economic efficiency and social equity.

On a general level, most do agree that there should be distinctions made in the timing and mechanisms for transferring various types of property -- i.e., land and real estate, small and medium enterprises, and large industrial enterprises. Privatization of small enterprises is already occurring at a very fast pace in many of the countries and seems to involve the fewest complications. The privatization of land has a more mixed record but as Marvin Jackson noted, this should be given high priority in order to rapidly improve the production and distribution of food. In this respect, Poland and Hungary have had some advantage as they both retained more decentralized agriculture than most of the other countries.

The transfer of large industrial state enterprises appears to be the most difficult for most countries, and the most complicated in terms of social considerations. One basic question is whether the transfer to private ownership should be immediate, or whether an intermediate stage of "corporatization" should occur, in which the enterprise becomes self-managing and self-financing before its sale to private owners, thereby establishing its viability. Although the latter approach has been advocated by some observers and is being used in Germany, Anders Åslund argued that speed in privatization is the most important condition for success; in his view, a critical mass of private enterprise must be established quickly within the economy before it will begin to work efficiently and without massive corruption.

A second basic issue of dispute is whether enterprises should be sold to new owners and the revenues used to bolster the state budget, or whether they should be freely distributed, with no concern for state revenues. Different views on this question were

expressed by the experts and different approaches are being pursued by the countries themselves. Beneath these controversies over the method of distribution lies the extremely sensitive issue of who benefits from privatization: should it be the state, the former owners of property, the population at large, the old elites, foreign investors, domestic entrepreneurs?

During the seminar, those involved in the privatization process in several countries described their respective approaches, highlighting the differences among them as each nation tries to establish an acceptable balance of equity and efficiency. In Hungary, most transfers will occur through market-oriented sales, with the State Property Agency as the seller, seeking competitive bids, assessing values and prices, and approving sales. While there continues to be sharp debate on the issue of compensation for confiscated property, this problem is not being given a central role in the privatization process. Likewise, some share of property may be turned over to local municipalities, but the issue of central versus local government control is not a central element of the program. While conceding that privatization is a "special market," the Hungarians are attempting to manage distribution largely on a market basis, with equal opportunities for foreign investors alongside domestic ones.

In the Czech and Slovak Federal Republic, market mechanisms are being supplemented with non-market distribution in order to address concerns of social justice. In particular, all former owners of confiscated enterprises (those confiscated during certain time periods) can reclaim them or receive financial restitution. Furthermore, the state plans to issue vouchers to the entire adult population that can be used to purchase stock in newly privatized enterprises. This system is intended to distribute wealth more broadly throughout the population and to prevent foreigners from obtaining too large a share of the country's wealth. In addition, it is hoped that the vouchers will promote development of an entrepreneurial class; some observers note, however, that if bankruptcies occur on a large scale in the next few years, novice stock-holders could well become more risk-averse, rather than entrepreneurial. One solution to this problem is to promote participation in mutual funds, rather than direct individual stock ownership.

The Polish privatization law relies primarily on the enterprise itself taking the initiative in transformation and privatization, rather than initiation by the central property agency or by a potential investor. This approach reflects, and is complicated by, particular characteristics of Poland's social and political relations. Because of the strength of the Polish workers movement and trade unions, the country's privatization process is particularly sensitive to workers' concerns and job security. In contrast to Hungary and the C.S.F.R., under Poland's law workers' councils in the enterprises have a virtual veto power over privatization. It was noted that the voluntary approach to privatization, combined with the strong role of workers' councils, seriously restrains the process and also discourages foreign investment. Moreover, other politically powerful social forces, such as the Catholic Church and the intelligentsia, are seen as obstacles to rapid restructuring of the economy and transfer to private ownership.

Yugoslavia shares some of the features of Poland's privatization with respect to the prominent position given to the workers in each enterprise. The Yugoslavian process of ownership transformation devotes special attention to workers' shareholding, which currently dominates among transformed domestic enterprises. While this kind of ownership is particularly suitable to the traits of the Yugoslav economy and its long emphasis on self-management, other forms of share capital and ownership are also encouraged. Foreign investment, through joint ventures, mixed capital companies, or fully foreign owned enterprises, is likewise being supported.

Finally, the U.S.S.R.'s process of privatization is also unique and reflective of its particular domestic constraints. The Soviet emphasis has been on de-statization, rather than outright privatization, meaning that control is transferred from the state to other entities, but the framework of state ownership remains. The methods of distribution remain under debate; the options are free distribution, sale based on a price determined by stock exchange and securities markets; or a combination of the two. Among the obstacles to be overcome are first, the creation of these markets that can effectively determine prices; second, the division of property between the center and the republic governments; and third, the development of entrepreneurial attitudes in a society long accustomed to viewing the state as its provider.

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Michael Silverman
Legal Advisor
Squire, Sanders & Dempsey

There are obviously a great many points of common interest, but also of difference, between the privatization programs which are being implemented in the countries in this region.

We are fortunate to have with us today three recognized experts who have actively participated in, as well as analyzed and studied, privatization programs and projects around the world. Without wishing to steal their thunder, however, I would like to make several points, as I have noticed that I am the only practicing lawyer on this panel.

First, in addressing this distinguished body of parliamentarians, I hope you won't think me presumptuous if I characterize you, the parliamentarians, as the lawyers, whether or not that is your educational background. You are the lawmakers, so simply, you are the real source of the legal profession. You are also the source and are at the core of the democratic structure. Without you, the executive branch of government

would have no laws to carry out or administer, and the courts' responsibility for interpreting laws would be superfluous.

In terms of privatization, your fundamental role of creating the privatization legal structure is very important, because to understand privatization, one must recognize the highly complex and interrelated areas of the law that are involved, that form the building blocks for any privatization program.

My premise is that, to design and successfully implement any large-scale privatization program, you as legislators are confronted with creating a sound and comprehensive legal structure. Mass privatizations of the kinds your countries are beginning to undertake will cut across almost all realms of economic and even social activity, and the laws governing these activities must be rationalized.

The privatization legal structure that I am referring to includes not only the corporate and commercial laws, and the laws governing foreign investment, which are usually discussed in the press and elsewhere as being the central elements of privatization, or even the securities and banking laws and regulations governing capital markets which many of you have already initiated. As a number of speakers have noted, privatization must also be reconciled with compensation laws, or laws relating to claims for previous expropriations or state takings. Obviously, these types of laws also go hand-in-hand with property laws, and laws which spell out the rights of ownership and use of properties. This is, of course, of critical importance to investors, both foreign and domestic, who need to be able to understand and rely on property and title rights.

But beyond these fundamental laws, privatization impacts on and affects, and therefore needs to be reconciled with, many other areas of the law, including patent and intellectual property protection laws; laws governing contracts, their sanctity, enforceability and interpretation; taxation, an obviously critical area ... for instance, whether an act of privatization itself is what we in the U.S. might call a "taxable event"; antitrust and anti-monopolies, or regulation of the competitive environment; bankruptcy, reorganization and liquidation, and the rights of creditors; and environmental protection laws.

I am not suggesting that you must or should even try to pass comprehensive legislation in all of these areas before you pass your basic legislation authorizing privatization, or before you establish the principles for undertaking a privatization program. There is great merit in actively beginning a privatization program before all of these detailed laws and regulations can be worked out. I do recommend, however, that when enacting your basic privatization laws and implementing regulations, you keep in mind the interrelationships between these fields of legal and economic activity. Your legislation should be flexible enough to permit the amendment and clarification of your privatization laws as your programs develop. And while you need not treat in detail with all of these points at the outset, you will make your lives as legislators

simpler and the lives of those who administer your laws and the private citizens who must abide by them simpler and more efficient if you include in your basic privatization legislation the fundamental policy points that you wish to see for these other, related areas.

The second and final point that I wish to make concerns the bureaucracy and administration of privatization. It relates to the legal structure as well, because, just as ambiguity and conflicts among the laws I discussed will lead to delays, frustration and a waste of resources in any privatization program, lack of transparency and conflicts in the implementation and administrative process will have the same result. One of the greatest complaints of foreign investors, and one of the surest ways to send potential investors looking for other homes for their funds, is for the bureaucracy which administers privatization to be perceived as acting in an arbitrary, unfair or even corrupt manner. In addition to economic factors, in large part the success of your privatization programs will depend on the fairness and consistency in their administration, and the perception of this fairness by the public and investors. Delays, political in-fighting, second-guessing and charges of unfairness, even possibly corruption, will result when the lines of authority of various government bodies or officials, in the decision-making process, are unclear or are in conflict. And it is here that the Parliament has a very important role, particularly its role of oversight. Of course, this is a very fine line, and you do not want to be drawn into micro-management, which itself will become the source of further delays and criticism.

Anders Åslund

Director

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After one year of transition to market economy in East-Central Europe it has become obvious that privatization of large-scale state enterprises is the most technically and politically complicated economic issue.¹ At the same time, it appears ever more vital to economic performance. The privatization of small enterprises, on the contrary, has turned out to be surprisingly easy (three quarters of Polish shops have already been privatized), while privatization of land and real estate are largely tainted with political obstacles.

Our perspective on privatization is framed by a large number of preconditions and considerations. A first question to pose is what we are to maximize. I would strongly argue that the main issue is to maximize national income in the long run. Therefore,

¹ I have developed this theme further in Åslund, "Principles of Privatization for Formerly Socialist Countries," Working Paper No. 18 (1991) Stockholm Institute of Soviet and East European Economics.

state revenues are pretty irrelevant. Moreover, short-term effects should not be given excessive importance.

A second point is that state enterprises function badly precisely because they are state-owned. We know that only economies with predominant private ownership have performed well in the world. Important reasons are that state enterprises have chronically soft budget constraints, and that state directors act more by political than economic criteria, as they are decisive for their careers. Thus, the task is to assure East-Central Europe of at least two-thirds of private ownership as fast as possible, without bringing havoc to society.

A third consideration is that the state administration in formerly communist countries is in extraordinary disarray and utterly demoralized. It is not likely to recover in the medium term. An obvious conclusion is that such a state administration is highly unsuitable to run any enterprise sector altogether, requiring a more privatized economy than would be necessary in a western economy.

Fourthly, a frequently neglected fact is that a very large critical mass of private enterprise is needed in a complex modern economy, if a sufficient degree of market balance and competition is to develop. The experiences of a private sector in Poland, employing more than one-third of the labor force but even so being utterly corrupted, suggests that this critical mass is likely to exceed half the economy. Thus, it is vital that a substantial privatization occurs as fast as possible.

A fifth point concerns the accumulation of risk capital. We have already pointed out that the state sector should be reduced swiftly. In addition, it is important both to stimulate private savings that can perform the role of risk capital and that this capital is used for real investments and not just paid to the treasury of the state. Then, we arrive at the conclusion that state revenues are not particularly desired, and especially it would be unfortunate if prospective entrepreneurs transferred their funds to the state rather than to new investments.

Finally, most state enterprises in East-Central Europe tend to be of much less value than has previously been understood, although the reasons are pretty obvious. With an investment process lasting for almost a decade, virtually all equipment is fairly obsolete already when it is installed. Furthermore, depreciation has been small and scrapping tardy, rendering factories both technically and economically obsolete. In addition, the autarkic tendencies have encouraged a concentration of all kinds of economic activities in huge conglomerates. In a market economy, it would often be self-evident to sell off hundreds of operations as independent firms. The chronic shortages have led to extensive hoarding notably of labor or over-manning that may be difficult to lay off. Many enterprises can hardly be justified in a market economy. The state has no good record anywhere when it comes to closing down superfluous operations. The obvious conclusion is that state enterprises are of little value to the state, while it

is vital that private hands may enter as soon as possible so that long delayed economic restructuring may start.

The self-evident conclusion is that the vital issue is that privatization should be just as fast as possible. The only assets of state enterprises that seem essential are human capital and land, and the human abilities will decline fast if they are not deployed in new activities soon enough. No fixed assets, good-will or market segments are so valuable that they are really worth bothering about. Nor are state revenues essential. A remaining argument for some caution is that dangerous social upheavals should be avoided, as they may wreck the whole transition process.

Still, the task boils down to maximally swift privatization, without bothering about state revenues. The obvious conclusion is that free distribution on politically acceptable terms is to be preferred, though as political barriers may prove formidable, it should be added that as many channels as is practical may be attempted. Two problems must be overcome. Ordinary people are risk-averse. In order to reduce the risks of the common man, it would be advisable to promote ownership of shares in mutual funds, pension funds or other social insurance funds rather than direct share-owning. Especially as half the state enterprises may go bankrupt within a couple of years, it would be politically unfortunate if half the population lost all their newly-won capital. They would be prone to become enemies of stocks as such.

Another problem is that the value of shares cannot be assessed before full-fledged capital markets have developed, and even then the evaluation of large enterprises is highly spurious as the swift and unexpected changes on any stock exchange make evident. This is a strong argument in favor of arbitrary distribution before a proper evaluation takes place.

My conclusion is that the advisable form of privatization is swift and massive free distribution of equally large shares of a sufficient but limited number of mutual funds to all grown-up resident citizens of the country in question. As a result, all kinds of capital markets will swiftly arise, with companies as well as mutual funds and individuals trading on the stock exchange. There will be room for creative destruction and constructive restructuring. The counter argument would be that these owners are likely to be weak, while particularly strong owners will be required for the restructuring. Alas, not all problems can be solved at once, and well-functioning markets are likely to generate and attract able owners faster than a degraded state economy. Unfortunately, the Czechoslovak voucher system seems to introduce the two unnecessary complications, excessive risk and evaluation.

The main alternative seems to be so-called spontaneous privatization, essentially implying that the managers and possibly workers of a state enterprise take it over at a low price. Frequently, it seems to be a question of management steal-out rather than management buy-out. The obvious objection is that such a procedure is highly unjust; it preserves the power of the formerly ruling class of communist officials and thus

arouses a public opinion against further privatization. Still, if we are serious about speed being the main objective, spontaneous privatization looks like the second best solution, especially considering that most state enterprises comprise very little real value. Moreover, the remaining alternatives would be sales through public offerings as in the West, which is bound to take a very long time as has already been proved to be the case in Poland, or sales to foreigners which easily arouse a strong popular reaction.

Marvin Jackson

Director

The Leuven Institute for East European Affairs

Parliaments in Central and Eastern Europe face difficult challenges in accelerating the agenda of economic transformation from planned to market economies. Most of their members lack either political or administrative experience since most came from among the ranks of the opposition to the communists and were excluded from leadership positions. The parliaments, themselves, are poorly organized. Most have to write new constitutions. Their political organizations are in disarray, waiting for the post-democratic restructuring around real interest groups, not merely opposition to communism. Besides, they face populations whose expectations are naive and badly informed.

Add to these issues of politics and law the great problems of readjusting technological, monetary and economic systems that were and still are badly disequibrated. It is easy to understand that it is absolutely necessary to avoid wasting limited political resources and energy by trying to create unworkable or otherwise misguided economic institutions and economic policies. Market economies and privatization require more than anything the clearing of impediments to individual initiative. That should be the focus of legislative action. Here are some key issues.

Avoid Economic Planning

In the early part of 1990 one could hear remarks suggesting the "French model of planning" ought to be adopted for the transition. In the same vein, a Romanian leader even referred to "Romania, Inc.", suggesting that because multinational companies planned, so should his country. But both comparisons are flawed. Almost no one, especially the French, believe the success of France's economy is due to its planning system. And the heavy exposure of multinationals to market forces make their planning quite different than would be the case in a whole national economy. Besides, when an economy is dying from the effects of over planning, it will not be made well by taking more of the same poison. The main legislative tasks should be to eliminate barriers to market forces and stimulate market agents.

Push the Rehabilitation of Small Farms

Clearing the way for market forces has no more urgent application than in the production and distribution of food. It was the luck of Poland that its agriculture was never collectivized. So stimulating market forces was mainly the freeing of prices and the reduction of distribution monopolies. Hungary's agriculture also had been significantly decentralized and exposed to market forces so it was possible for both Poland and Hungary to quickly relieve some pressures in the early stages of transitions with rather well-supplied food markets. Contrast their case to the situations prevailing in Bulgaria, Romania, and the Soviet Union throughout 1990. The official policies of attempting to control prices at below-cost levels and of attracting so-called "speculators" and "black marketeers" was a clear effort to cater to popular prejudices. It merely drove the available supplies into informal channels, even significant unrecorded exports for hard currencies in the cases of Bulgaria and Romania. Legislative efforts should clear the way by freeing food prices and farm land for private cultivation. The result will be not only a quick supply response, but also an alternative employment for redundant workers.

Subsidize Incomes Directly

There is unfortunately no way to avoid the costs of over-industrialization and neglected modernization inherited from the communists. There is, however, a cheaper way to subsidize the incomes of workers in such industrial enterprises than to subsidize their employment. If this is done, two costs must be paid: subsidies to keep enterprises operating in spite of high costs or unsaleable products and the costs of energy, raw materials and even labor force that either would not have to be imported or could be otherwise occupied. It is better to pay the workers in such cases direct cash benefits. And it would be even better to look the other way if they decide to re-employ themselves in the private sector. If prices in farming and construction have been freed, many of the unemployed will find themselves new occupations. And the rest of the society will benefit from added production of goods that are really wanted.

Promote Small Enterprise

If parliaments are looking for ways to keep persons employed, they really should consider what is missing in their economic structures. Comparison of average enterprise sizes will quickly give the answer. What is missing are the thousands of small- and medium-sized enterprises that form large portions of all enterprises in the West. In the German and Belgian economies, for example, medium-sized enterprises in the machinery and equipment branches provide some of the most efficient exporters. In addition, studies of technological change in the West usually show that large proportions of innovation take the form of small companies that are formed by the innovating engineers. Besides, which would be easier: to pay for the reconstruction of "red elephant" combines or to stimulate the establishment of brand new small-scale enterprises?

Don't Give Workers the Dinosaurs

A problem will be that some workers in those "red elephant" combines will demand the right to take them over. In general, there is great political pressure, in any case, to give workers considerable rights over the future of the enterprises in which they work. But parliaments who give in to these demands are creating major political problems down the road when it turns out that many of these enterprises produce intolerable pollution or simply can not make a go of it without subsidies. Democracy and codetermination do not mix easily with industrial restructuring. So wiser parliaments will try to do the restructuring before they give in to worker demands for ownership or codetermination.

George Vojta
Executive Vice President
Bankers Trust Company

I would just like to make two or three basic points about some of the financial implications of privatization which perhaps might round out the perspective, that I think are of importance to be concerned about.

The first point is that privatization in your economies is an opportunity to recapitalize your economic enterprises in a sound fashion and, in addition, to improve the overall fiscal position of the state. And thirdly, in some countries around the world, it is also a possible opportunity to do something positive about the burden of external debt that is weighing on the country.

When we privatize, of course, we are taking the burden of deficits off the state's hands and should make a great improvement in the fiscal position of the country. Secondly, the capitalization of the enterprises will have, we hope, sufficient equity capital that further burdens in financial terms can be avoided and that as many as possible of these enterprises would be able to be financed on an ongoing basis from the marketplace--from the banks, from the securities markets, and so on. Thirdly, many countries around the world have used mechanisms called debt-for-equity swapping to permit foreign investors, in particular, to use the countries' external debt as a currency of exchange for the purposes of acquiring an equity position in an asset in the country they wish to invest in. And where that has been done successfully, a substantial reduction in the net external debt has occurred and there has been a source of capital for the local investment that has been converted to equity. As a result, the economy as a whole has been de-leveraged. And so as you think about how to finance privatization going forward, consider the experience around the world with debt-for-equity transactions involving your external debt because I think there is a role for that.

Finally, let me say this. We all know that, in going forward, a financial marketplace within the country, banking reforms, the development of capital markets are very important. We must have those as a way to support the development process. The privatization of companies will stimulate the financial reform in the banking sector, in the capital markets sector, that will be necessary to support the further growth of the country and so it is a reinforcing thing. And I think you should see therefore there is one other opportunity of privatization, the chance to promote appropriate financial reform in your economies.

VIII. MONETARY STABILIZATION

Highlights and Commentary

Monetary stabilization is an important condition for successful reform and restructuring of the economy and has been made the first priority of several transforming countries. However, establishing monetary stability through price reform and reduced government spending may conflict with other important objectives and may also undermine popular support for transformation. The tasks of monetary stabilization and fiscal policy include both liberalizing prices and establishing fiscal discipline. The difficulty lies in eliminating old institutions and practices, including state subsidies, without losing control over the money supply. New institutions such as an independent central bank, competitive commercial and private banks, and a modern tax system will be critical for managing the transition. Moreover, mechanisms for capital formation and (ultimately) currency convertibility are major requirements of a well-functioning market system.

The development of banking institutions is a crucial condition for the transition to a market economy. A competitive commercial banking system is necessary to promote domestic savings, and to allocate these savings to businesses, based on judgments of profitability and efficiency. In the view of Paul Volcker, an effective commercial banking system must be characterized by efficiency, independence, and diversity. Well-functioning financial institutions are also necessary for attracting foreign investors.

Besides competitive commercial banks, the transforming countries would benefit from the development of strong and independent central banks. While the specific functions of central banks in Western countries and their relationships with government may differ slightly, the participating central bankers all agreed: a central bank can be essential for maintaining monetary stability and controlling the money supply. It can be a valuable instrument of monetary policy, preventing inflation and providing fiscal discipline. However, the powerful instruments of a central bank (interest rates, reserve requirements, etc.) also may be used to support policies in conflict with the goal of monetary stability. As the bankers noted, when governments come under short-term pressures, they may look to the bank for deficit financing or interest rate adjustments.

For this reason, central banks must be strong and independent of government, able to withstand such conflicts and pursue medium- and long-term policies. In formal terms, "independence" for the central bank may be defined differently -- the central bank is not completely isolated from politics; at the least, its leaders must remain responsible to the democratically elected government to justify their policies and actions. Nevertheless, several components of independence appear essential, if the bank is to fulfill its functions of maintaining stability and confidence in the nation's financial system: the central bank must not fund the fiscal deficits of the government; its officials should have long terms of office; and its staff must be professional, non-

political and expert. Moreover, the effective functioning of a central bank also requires an acceptance not only by the government, but also among the population, of the goals of price and monetary stability as necessary conditions for economic growth.

The countries of Central and Eastern Europe are beginning to develop banking legislation and the foundations for a competitive commercial banking system, but the process is only in its early stages, even in the most advanced countries. Though there is a general recognition of the need for a strong central bank, the existing central banks continue to fulfill the old role of funding the central budget, along with new roles in supervising the creation of new, competitive banks. A common problem in the establishment of financial institutions is the shortage of qualified, knowledgeable personnel.

* * * * *

Paul Volcker

Chairman, James D. Wolfensohn, Inc.
Former Chairman, U.S. Federal Reserve System

I just arrived, but it is a beautiful spring day and a very dramatic building.

There are enormous changes, I am aware, in Eastern Europe generally, and in Hungary in particular. They capture all our interest, all our imagination, and I'm sure what's going on in this part of the world politically as well as economically is going to have a large bearing on the direction of the entire globe well into the next century. I know there is a tendency in my country to think that success is assured, that anybody moving toward a market system and democracy and human freedom is on the right side of history. But I think we also realize, in our more sober moments, that it is a difficult process. Expectations are high, but it's going to be years before expectations in the economic area, at least, can be met.

I've been asked to talk about rather technical things about central banking and monetary policy but I want to say and emphasize first more fundamental changes are necessary than changes in the banking system -- Fundamental changes in psychology and economic and political institutions and law. It's going to be difficult to mobilize capital, and to mobilize technology, in the amounts needed, before those other really more basic changes are made. Capital and technology are a technical problem. I think we know how to solve those needs, but there really isn't much precedent for moving from a centrally planned economy into a free political and economic system. Before I start, let me say too I think you should be skeptical about visiting experts who come in here for a day or two whether they can really tell you much about what is necessary.

People in Eastern Europe seem to be embarked on really unprecedented changes in areas where none of us are expert.

With that much introduction and reservation about what I can really tell you, I must also say, I believe from my past contacts that you in Hungary are in a relatively good position to make the very difficult transition. Hungary started much earlier than many other countries in Eastern Europe. I know that all of us in our life in the West come into daily contact with Hungarian emigres and we have no doubt that a spirit of enterprise and ingenuity hasn't been lost. I think you have a foundation upon which to work.

I look forward to this discussion about central banking and monetary and fiscal policies and what they can do to facilitate the transition to an efficient, flexible, effective market system. I know there's going to be a lot of room, a lot of time for discussion. I just want to raise a few very broad questions and some broad solutions to stimulate the discussion.

In that connection, I can't help but start by raising one basic question, I observe what is going on in Eastern Europe and in the U.S.S.R. (not only in the U.S.S.R. as a whole but in the various Soviet republics) and in China. Apparently everybody wants a central bank and everybody has attached a great deal of importance to having a central bank. That makes me wonder a little bit. It is not that I doubt the importance of central banks. I have spent 20 years of my life in a central bank and I have associated with many central bankers and I have great respect for central banks and central bankers. The Federal Reserve, I like to think, plays a great role in the United States. But it is also true, if we look at the broad sweep of history, that central banks have been fairly obscure institutions historically and they have arisen, actually, at a fairly late stage of the market economy.

The Federal Reserve System in the United States was only created in 1914. The Swiss National Bank--and we all think of Switzerland as having a historic market system and great stability--was only created in 1907, if I remember correctly. The Bank of Canada, the central bank of Canada, was only created in 1935. The Bundesbank was created perhaps a hundred and fifteen years ago, in rudimentary form, still in the broad sweep of history, fairly recently.

The point I am making is that I don't think a central bank is essential to a market system historically. What is really essential if you look backwards, is a commercial banking system. You do need a system of institutions, presumably privately run, which will compete for savings -- compete among individuals and among businesses to attract liquid savings -- and then redistribute those savings profitably to businesses that can use the funds efficiently and effectively. I really think that process is quite different from the pattern of the controlled economies in which the banking system is quite subsidiary to a state plan. The state banking system did not have much authority except to carry out the state plan. It didn't have to worry if its loans were good or bad;

it didn't have to worry about what interest rate it was paying. It was not a system, in my opinion, that bred efficiency, independence or diversity.

If you are going to have a market system you need a system of efficiency, diversity and independence. You need competition, you need skills, in the provision of credit, you need to make judgments about what businesses are efficient, or likely to be efficient, and what businesses are inefficient. You need a system of risk and reward. All of that, in my judgment, requires--as an absolute matter--a good, efficient, competitive banking system.

In the Western world, and in market economies, we have had a banking system for hundreds of years. When you have that competitive banking system, interest rates become very important. They have to be able to move freely because they are the tool for the allocation of capital, they are the main tool for attracting savings. So I think it is absolutely essential to have a good banking system and a good system of financial institutions generally.

But I ask myself, why is it so important to have a central bank? Well, in raising that question, let me say there are a few things central banks can do and do, although not every central bank in every country does all of these. If you have a banking system, I think experience has shown you need an organization to regulate the banking system and supervise the banking system. You need somebody that can do that with efficiency and capability. Typically, that is a job for the central bank.

It's also true if we are going to have an efficient system of savings, an efficient system for making payments, there has to be some way of transferring money efficiently -- transferring money from one account to another (which you must do not just in one bank, but from one bank to another and from one country to another). Typically, the central bank provides that service of handling payments between banks.

Every country, if it is going to participate in international trade and international finance, needs some institution to manage its international financial affairs and its financial contacts with other countries, to hold international reserves, and to hold other currencies, to borrow money abroad. That is, typically again, at least part of the job of the central bank.

Finally, I think, countries need good and intelligent economic research. They need a place of unquestioned professional standing to provide economic research. They need a place where economists can be trained and again, in many countries, that is at least part of the job of the central bank.

All those responsibilities together in differing amounts in different countries, they all add up to very significant responsibilities. Collectively they're very important; and most of those duties, or all of them, are done by a central bank.

Nonetheless after repeating all that and saying it's very important, it is hard for me to say that all those particular things are so crucial they require priority in creating a central bank. Other agencies can do those things. Why then is the central bank given so much attention in these new market economies?

Well, of course, the really crucial function of a central bank, the thing that can't so easily be delegated or done by others is to control the supply of money in the economy. The amount of money in the economy can have profound effects. It certainly influences interest rates and there is always a lot of concern about interest rates. The control of the supply of money also sets limits, typically, on how much the government can borrow. The government will have to fit its borrowing program within whatever limits are set on the creation of money. Increasing or decreasing the supply of money will affect investment through interest rates or otherwise. It will affect overall economic activity. It will affect employment, what it will also do, with great certainty, is affect the inflation rate and the price level over time.

Having said that, having a central bank is not the only way to control money. Obviously we controlled money in the United States before 1914 and the Canadians did in Canada before 1935. And all those German municipalities and principalities did so before 1875.

In concept we could have the gold standard. We could have currency boards with the amount of money limited to the amount of foreign exchange that is held. A nation could join a bigger currency unit, as is being discussed in Western Europe now. A country could, in fact, use another country's currency as Panama does, as Liberia does, as is occasionally discussed in other Latin American countries. So you don't really, in some theoretical sense anyway, need a central bank.

I might also say that the control of money is never very precise, or at least it is not very precise in its effects. Some countries may do it better than others. Moreover, in any country, all these different objectives and influences I have mentioned may conflict. There may be, or appear to be anyway, a conflict between stimulating the economy and stimulating investment and keeping prices down or stabilizing prices. There may be a conflict between limiting the financing of the federal government and the spending that parliament might want to do. It is the nature of the problem of controlling the money supply that one has to try to balance out different objectives. In particular, one has to balance out short-run, particular objectives from what may be good in the long run. And there no doubt are long lags between an action today or this month to change the money supply and what happens in the economy, and sometimes those lags may take years.

What I am really saying is that the essence of a central bank is that it is an absolutely crucial instrument to national economic policy. My interpretation of why everybody is so interested in setting up a central bank is that it now is considered an

inherent instrument for national economic independence, for national policy autonomy. Its power is potentially enormous.

The potential of a central bank for doing good, I think, is very large, but its potential for doing bad is also large. And if policy is not intelligently conducted, if there is not adequate discipline, the power of money creation can be abused and will be abused in a manner that is contrary to economic performance. We have many examples of that, historically. Before there were central banks, the sovereign found many devices for increasing the money supply. Back when they had gold coins they used to clip the coins, so that each coin would have a little less gold and the fixed amount of gold went further. Of course the result was inflation.

In modern central banking we have more examples of money creation running out of control. When you are in North America and you look at South America, you see a very sorry history of countries that have central banks, but they are not functioning very well. They have had a record, a long record over decades, of inflation. And by and large the inflation has tended to get worse instead of better -- until recently, until the last decade or so. I think it is fair to say that, very broadly, as the inflation got worse so did economic performance. But the temptation is still very strong sometimes to try to increase economic activity in the short run at the expense of inflation. In the long run, you accumulate undesirable performance.

Let me say two or three things about central banks that I think grow out of a lot of experience in recent decades. I think it is true that while performance has been uneven, in particular instances in many countries -- and I like to think the United States is one of those countries -- the central bank has achieved a certain respect that is really almost unique among governmental institutions. I would cite the Bundesbank as one example of that. In Europe it is considered a kind of repository of non-political, independent expertise about the economy and about economic policy.

We are never going to remove the politics and the controversy from economic policy. You are talking about important things that affect people. In the end it shouldn't be removed from politics in the broadest sense. But I think the fact that economic policy is so apparently controversial makes it all the more important that there are some institutions, at least one institution, that can be respected as a neutral and expert source of analysis. I think that is the role the Bundesbank plays today. I think it is a role at the other end of the spectrum in terms of formal legal independence, that the Bank of England has played for a long time. The most remarkable example, it seems to me, in Europe in recent decades has been the Bank of Italy. The Italian government, as you may realize, has historically had difficulty in having a strong and coherent economic program. The country may be quite democratic but it is not very disciplined in its governmental programs. The Bank of Italy has been a consistent source of stability and expertise in that country and I think the performance of Italy through the years--which has been quite brilliant really in economic terms--owes a great deal to the stability and professionalism of the Bank of Italy. To take another example from a

quite different part of the world, a quite different stage of development, I would point out to you the Bank of Mexico. The Bank of Mexico, because of some particular historical events, has had a very strong professional tradition. It is not, in a legal sense, completely independent but it has had an enormous amount of influence in Mexico through many decades based, I think, upon its competence, the competence of its leaders and the competence of its staff.

If a central bank is going to play that role, and I think it is a very important role, it is obviously a lot easier if it is provided legally with a certain amount of independence and a certain amount of continuity and a certain ability to finance its own affairs. I might emphasize to you those same qualities of professionalism, continuity, intelligence, and competence are extremely important in maintaining credibility with its counterparts in other countries. That may not be important at all times, but at a time of crisis, at a time when loans may be necessary on an emergency basis or otherwise, the credibility and independence of the central bank can be a vital ingredient in maintaining the stability of the economy at home. And I could cite both the Bank of Italy and the Bank of Mexico that within recent decades have played an absolutely indispensable role in that respect.

In the end, the really crucial question is how monetary policy is run, how the money supply is increased or not. As I indicated, the temptation to increase the supply of money is quite clear in all of history--the temptation to create more money to finance a government deficit instead of reducing spending or increasing taxes; the temptation to create more money to stimulate investment and to stimulate the economy, even the temptation, in the short run, to promote the interest of one political party or another that may happen to be in power at some particular point in time. It seems to me all those temptations and all those pressures are bound to arise in countries moving in very difficult circumstances from a controlled economy to a market economy. They have, on top of all the normal pressures, the very great difficulty of moving from a system of controlled prices to a system of free prices which will almost inevitably produce a short-term inflationary outburst. It becomes a very important question how to avoid the immediate inflationary pressures, which may be inevitable, from becoming a long-term problem. The importance of dealing with that kind of situation, it seems to me, is the real justification for all the talk about the importance of a central bank. It is also justification not just for a central bank, but for a strong central bank. Otherwise it is not going to do you any good.

What do I mean by a strong central bank? Well, there is a lot of discussion these days about the meaning of providing a central bank with independence. What do we mean by independence? We mean clear authority within itself to take decisions. It means, in most countries, long terms for the people running the bank. Long terms of office usually implies being run by a board and not by an individual. It means the people running the central banks should not be politically partisan. In many countries, like my country, and in Germany, it helps to have regional links so that the source of support is not always from the central authorities, but that there are also roots around

the country. It certainly is important, as I emphasized earlier, that whatever the legal structure, a central bank may have a highly professional staff with an interest in their professional reputation and an interest in continuity.

You can help all those things by legal structure. But I must say, more important than the legal structure is a state of mind -- a state of mind among the population as a whole. Is the government, are the citizens of Hungary or any other country, genuinely convinced of the importance of price and monetary stability to their economic future?

It seems to me that is the lesson of history--that it is terribly important to create a stable monetary environment if you want consistent growth. In country after country we have learned that once stability is lost, it is extremely difficult to restore. That's been true in modified form in the United States. Latin America is a much more obvious case in point. It is true today in the United Kingdom. There are some examples, on the other side -- Germany and Japan to name two, that have been relatively successful in maintaining stability. I don't think it is any accident that their economic performance by and large has been good. It is a particularly great challenge among many of your neighbors. It is going to be a huge challenge in the Soviet Union.

I think it is important for Hungary and the other countries to leave no doubt about a very basic decision. And that decision is that you are creating a central bank with the primary purpose and responsibility of maintaining price and monetary stability.

A central bank is a two-edged sword. It can be a great force for good, but inflationary money creation can undermine and destroy good economic policy as well. The temptations are going to be strong here, as they are elsewhere, to create too much money. I urge you during your deliberations to give full consideration and importance to monetary stability and the arrangements that are necessary institutionally to create and maintain a central bank that will defend that stability.

Helmut Schlesinger
President-designate
Deutsche Bundesbank

What is the essential role of central banking in the process of transforming a centrally planned economy into a market economy and how important is the independence of a central bank in this context?

Regarding the first question: What is the essential role of a central bank, if the economy is conducted by market forces and no longer by the central plan and the commands of the government and bureaucracy?

The essential role is to keep the value of the currency stable. L. Erhard, who introduced the market economy into West Germany, always expressed the view that the population must be able to trust the currency and therefore inflation must be avoided.

In the event of inflation, the price mechanism cannot fulfill its task of steering the economy. That means helping the decision-making process in what to produce, what to sell, which prices to ask for and which level of wages is compatible with competition.

And, finally, inflation means that there are not enough incentives for private saving, not enough capital formation, no assurance of an optimal use of capital.

The production of money in our present financial system is--technically speaking--not complicated. But money supply has to be kept tight and has to be kept within the limits of the possible expansion of the supply of goods and services. Only the central bank can try to keep the supply of money and the supply of goods in equilibrium. At least, among all government agencies, the central bank is the agency which is best prepared to do this--or at least should be.

For that target--avoiding inflation through monetary policy--the central bank must have the necessary instruments and should be independent as far as the use of these instruments is concerned. I will not go into the description of the instruments; these are--so to speak--technical questions. Instead, I want to go into the details of why, in my view, a central bank should be independent.

Let me first try to explain what independence of a central bank means.

Independence of a central bank is its right to use its instruments (interest rates, minimum reserve requirements, etc.) to reach its target of avoiding inflation without interference by government orders. In other words, an independent central bank does not operate outside the political world. As our Bundesbank Act states, the central bank has to support the general line of the government's economic policy--as long as this does not contradict its primary target.

Here we come to the possible conflict situation of a central bank. One has to answer the question why the central bank should be independent. In my view, conflicts have to be solved in favor of monetary stability. And those conflicts arise mainly because politicians may feel it is easier to solve problems with the help of the central bank than without it. For instance:

- to finance the budget deficit;

- to solve particular difficulties in the economy by low interest rates or even by direct credits to specific enterprises or sectors of the economy (export industry, housing, agriculture);

-- to push down the interest rates in general, to bring them below the market rate in order to give a stimulus to the economy, which helps in the short term only and brings inflationary tendencies in the longer term.

The central bank has to act against those wishes. An independent central bank can do this and can take some of the unpopular measures which the government would otherwise have to take, but would hesitate to do. In fact, an independent central bank is--in the longer term--a big help for the government.

One is very often asked how an independent central bank can be kept democratically responsible. I think this question has been considerably overemphasized by those who are against an independent central bank. In fact, a central bank operates within the framework laid down in the relevant legislation and has to explain regularly to the public, parliament and the government how it intends to fulfill its functions.

If the ways in which it seeks to use its power are unsatisfactory, the central bank law could be changed just like any other law.

Keeping a central bank really independent depends not only on the law and formal regulations. It also depends on the people in the bank's decision making body. The government has to select people who can be independent: by their nature, their knowledge, their freedom from invested interest in the economy, in the political life of the country. And, they must have a clear status, for example, they cannot be dismissed at short notice, they should have long-term contracts.

A last remark regarding the link between an independent central bank and its banking supervisory function. There is no question that a modern banking system needs regulation, mainly in the interest of smaller savers and the soundness of a country's financial system as a whole.

Another question is whether an independent central bank should have the full responsibility of banking supervision, which implies having the right to close a bank if necessary, to ask for the dismissal of the responsible bank management, to ask for sanctions, etc.

My personal impression is that this is not the ideal combination. If a central bank is independent, it cannot or should not act like a government authority, like a court or like a bank policeman. The German practice is to leave the authority to a government agency. The central bank acts only as an agent; it brings in all its expertise, but it has no authority of its own in this field. My attitude is influenced by the observation that an independent central bank can keep its independence even in the event of a bank failure. It should not be forced to try to save a bank by providing central bank money if there is no very strong case for doing so; there should be no conflict between its supervisory and its other central bank functions, its main function, to keep the value of the money stable.

Philippe Lagayette

First Deputy Governor, Banque de France
Former Member, EEC Monetary Commission

I will simply try to add some remarks because it is, as you can imagine, quite hard to talk about what a central bank has to do, or must not do, after two excellent speakers. We have to keep some humility because if you look at the various central banks in the Western countries, you see some differences in their activities, and their legal situation. But, I think it is true to say that there are some basic principles in the functioning of Western central banks and those principles could be also useful for countries which are now moving towards a market-oriented economy. Let me focus on two issues.

First of all, one which has been already touched upon is the importance of monitoring money supply. Yesterday, John Williamson pointed out very rightly that nowadays a growing economy is an open economy. And, the prospect of convertibility of the currency in that open environment is necessary quite rapidly. Monitoring money supply is required to monitor the exchange rate which is going to play a key role in adjusting domestic competitiveness and regulating capital movements.

Secondly, among the bad advice you could have received a few years ago, from which I hope you have escaped, is the idea that inflation does not matter a lot; and that even inflation would be something necessarily associated to growth. You could have heard such opinions maybe 15 or 20 years ago but now, because our economies are much more and always more open, you will not hear that any more: an inflationary economy has a structural disadvantage in the competition. This reinforces the importance of correctly monitoring money supply. And in a democratic country, the responsibility for that monitoring has to be kept at a certain distance from government because it requires a medium term view and has to be somehow protected against the temptation of creating too much money, under the need of solving immediate and pressing problems. This is the primary function of a central bank. So, a central bank could be called a special precaution that democratic countries take with the currency. Only democratic countries can do that and have the requirement to do that. It does not mean that a central bank is isolated, as Helmut Schlesinger has very correctly explained. But it means that the ultimate responsibility about the currency is precisely located. In that respect one point must be clear even if the relationship between government and the central banks varies from one government to another, from one country to another: the central bank must be out of the business of direct financing of government deficits. This is the key point for a significant degree of independence of the central bank.

I will now turn to another point. As Paul Volcker said, more important than having a central bank is to have an efficient commercial banking system.

In a market economy, the decision of extending credit is a key decision which must be made by independent people on the ground of profitability and efficiency. It is why this kind of decision rests in the hands of commercial banks, which have to remain safe and sound. It is therefore necessary that commercial banks be required to assess the consequence of their credit decision on their profitability and financial structure. For that purpose, the central bank can help. There must be a minimum of regulation and oversight of commercial banks, in the hands of the central bank.

The central bank has certainly a responsibility in overseeing the safety and soundness of the financial and especially of the banking system for another reason: there cannot be a monetary policy aimed at stability if there is no confidence by the general public in the safety of deposits and storage of value in the banking system.

The central bank, when it performs monetary policy, must be able to move interest rates. It is one of the most instrumental decisions. In order to be able to move interest rates the central bank must be sure that the financial system, and the banking system, specifically, can bear it. That is to say, that there is no weakness of the banking system, such that a move of interest rates could have disastrous consequences.

Of course, there is a tradeoff between safety and dynamism of the commercial banking system. Too much regulation certainly kills dynamism and finally also kills safety because safety comes in a substantial part from profitability.

Despite this tradeoff, a certain degree of regulation must exist. The first essential area of regulation is for the central bank to be able to license commercial banks individually. The central bank must also be in a position to ensure a certain degree of competition between commercial banks. It is essential not to have too much specialization for commercial banks, because specialization encourages borrowers to consider banks simply as a window to provide them with the funds they think they need. Competition between banks is needed to help both banks and enterprises to behave rationally.

There must also be minimum conditions required for accounting regulations of commercial banks so that the central bank correctly assesses the situation. We know in Western countries how difficult it is to assess the situation of commercial banks. For example, the definition of non-performing assets is a very important element of this accounting regulation. There must also be a minimum of liquidity rules, a solvency rule, and in that respect a certain amount of own funds for capital is a key element.

And finally, the central bank is normally in charge of banking supervision to check whether all those regulations are applied by commercial banks. I think, contrary to what my friend Helmut Schlesinger said, that there are certain merits to concentrating this responsibility of supervising the commercial banks in the hands of the central bank, especially in countries in which big reforms of the commercial banking system

are undertaken and especially also if there is a certain shortage of expertise in the area.

Let me conclude, Mr. Chairman, by two words which are necessary for any country which wants to progress in developing its economic effectiveness, and also two key words for central banks. The first one is stability. Stability of the currency and also stability of the banking and financial system which is absolutely necessary in economies in transition as well in economies already quite well developed. Having a central bank sufficiently independent does not give the complete assurance to maintain stability, of course. But let us say that it is a good way to have a better chance to get it.

And the second word is credibility. The most precious asset for commercial banks is public confidence. To succeed in bringing monetary stability requires confidence as well as maintaining stability of the banking system. Most of the economic mechanisms and reforms which have to be put into effect crucially depend on public attitudes to finally work or not work. And when this confidence is sufficiently well established, credibility comes and helps.

Jean-Jacques Rey
Vice President
Bank of Belgium

I am grateful for the privilege of addressing this prestigious Conference. As a Belgian, I am particularly sensitive to Hungarian hospitality: as you know, we used to share the same monarchs back in the eighteenth century; we now share the same Executive Director in the IMF and the World Bank. That may involve some scaling down in appearances, certainly not in friendship.

There is not much to add to what previous speakers said about central banking. I would like to limit myself to two remarks, which are not offered by way of generalizations, but which are drawn from the specifics of our own experience.

First, it should not be taken for granted that monetary policy implies in all circumstances the exercise of some control on money supply. In a small open economy, like Belgium's, it may be advisable, provided the fundamentals are broadly in order, to seek stability in the exchange rate rather than in the growth of money supply, as the intermediate target on which monetary authorities focus their attention. On the real side of the economy, the rationale for this lies in the size of the import content of final demand: as a consequence, import prices are a major determinant of the domestic price index, both directly and through the price-wage cost relationship, as well as of the domestic cost of export goods. On the financial side, the credibility of the exchange rate commitment can help bring down the risk premium incorporated in the interest rate

differential needed against the reference foreign currency, to make sure that capital flows play the desired equilibrating role.

Indeed, in a highly integrated world, where capital flows freely between currencies, the impact of interest rate moves on exchange rates clearly increases relative to the impact of such moves on domestic spending. Admittedly, the ultimate logic of this reasoning is to set up a monetary union with the country issuing the reference currency, and to merge the central banks. As you all know, this is on the agenda of the European Community. In the meantime, the selection of an exchange rate target in a small open economy is a well reasoned option.

The selection of an exchange rate target implies the pegging of the domestic currency either to those of major trading partners or alternatively, to one important outside currency, for instance in the case of Belgium, the DM. On experience, pegging to a basket carries a lower credibility in terms of anti-inflationary policy than pegging to a currency that qualifies as an anchor of stability. Whatever the anchor, pegging the currency will act as a constraint on policies and enhance confidence only if it is associated with an unrestricted convertibility, at least for current account transactions, a necessary condition to ensure the integration of the economy into the world price and trading system.

My second remark hinges on the problem of reconciling the pursuit of a meaningful monetary policy and the financing of a significant fiscal deficit. Beyond a certain point, no central bank, however independent on paper, could probably prevent the direct or indirect liquidity effect of a fiscal deficit, and to that extent, an obvious priority is clearly to bring down the deficit itself. It matters a great deal, however, whether the Treasury is able to fund its borrowing needs on a developed and efficient capital market, involving the broad participation of non-banks, particularly institutional investors. In other words, it may not be enough to devise an autonomous central bank and a competitive commercial banking system to safeguard the pursuit of a monetary policy geared to price stability. The tasks of monetary and fiscal authorities can only be kept separate when a broadly based capital market serves as a cushion between the provision and regulation of liquidity on the one hand and the channeling of savings to borrowers on the other hand.

Belgium has recently experienced the merits of this simple truth by taking the opportunity of a major drive to improve the functioning of the financial markets, both long term and short term, to overhaul the operational instruments of monetary policy and cut to virtually nil the access of the public sector to central bank financing. The benefits are not only to allow a clearer delineation of the responsibilities of the central bank and the Treasury, but also to ensure that public debt is funded at more competitive conditions. To be sure, this was only possible after bringing down the fiscal deficit to a level which, though still too high, was no longer inconsistent with sound macroeconomics, as witnessed by the surplus on current account and a high degree of price stability.

IX. SUMMATION

Highlights and Commentary

The issues facing Central and Eastern European parliaments as their countries undergo transformation are complex and encompass many difficult choices. As the questions raised in this seminar suggest, there are no single or simple solutions to the problems of political and economic transition. But by engaging in open debate over the alternative solutions, and bringing to light the trade-offs they involve, the parliaments may work toward establishing a consensus on which transformation programs can be anchored. Each country may draw lessons and ideas from Western experience, but according to its own requirements and conditions. In moving toward conformity with international norms and criteria, each country may be expected to take its own path.

Still, the general challenges facing each of these countries are the same. And in resolving the challenges of transition to democratic market systems, the parliaments of Central and Eastern Europe face a special responsibility. As the link between the population and its elected government, parliamentarians must work to forge a broad consensus around the comprehensive programs of transformation. They must act as a channel of communication between their constituents and the government, on the one hand explaining to the population the need for new, often painful, economic policies, and on the other hand, considering the electorate's needs while fashioning legislation and economic programs.

While the seminar showed broad acceptance by the parliamentarians of common objectives in transformation and a common agenda of major issues and trade-offs to be resolved (as reflected in the panels and framing paper of the meeting), there was considerable divergence among them regarding which methods and choices would be most successful for attaining those common objectives. Nevertheless, the common ground that was established may be useful as a basis for further discussion. Through smaller working groups, focusing on narrower topics and involving not only parliamentarians but also representatives of the multilateral institutions, banks, business, and Western governments, it may even be possible to develop a common framework or criteria for assessing the progress of transformation. Such a continuing dialogue could be extremely constructive and could contribute to cooperation among the countries of the region and between them and the West, enhancing the prospects for successful transformation in Europe.

* * * * *

Charles McC. Mathias

Vice Chairman, Board of Directors, The International Foundation
Former Member, United States Senate

When the International Foundation joined with the Hungarian Parliament to plan this conference I had very high hopes, because I had had one previous happy experience with the Hungarian Parliament. Five years ago when I was the president of the North Atlantic Assembly, the parliamentary branch of the NATO organization, we took the decision to make what we then called "an opening to the East." Moreover, our opening to the East was a very modest gesture indeed. It was in fact no more than a visit that I paid to the Hungarian Ambassador in Washington, asking him to transmit to the Hungarian Parliament the suggestion that we develop some dialogue between NATO and the East, and specifically between NATO parliamentarians and the North Atlantic Assembly and the parliaments of Eastern Europe.

That small step was extraordinarily successful. Last fall I visited the London session of the North Atlantic Assembly, and there I found official delegations of observers from Yugoslavia, Bulgaria, Hungary, Poland, and Czechoslovakia--from the whole of Eastern Europe. It was extraordinarily rapid development of the dialogue that we had projected on such a modest basis just five years earlier. So I express my gratitude not only through this conference, but for all of the initiatives that have been taken here in Budapest in this extraordinary period of history.

I want to speak very briefly, so I will omit any of the oratorical flourishes that people expect from parliamentarians, and talk to you very directly as colleagues.

It has been my observation that service in parliaments has three aspects: one, which is obvious, to legislate; secondly, to educate; and thirdly, to advocate. And legislation includes not merely the enacting of laws and then leaving them to work their way alone and to make their own fate, but it includes the oversight of the administration of the law. You can't just enact it and then walk away from it; you have to see that it is properly administered.

It seems to me, that many elements of the economic environment are the primary responsibility of parliaments. There is taxation, there is the authority to borrow, there is the authority to appropriate public funds, and there is the responsibility to make the rules for commerce. In periods of transition, as we have heard through these last several days, there is a requirement for a great deal of courage and a great deal of nerve. You need the courage to adopt the policies and enact the laws, many times without any certainty that you will achieve the goals that you seek. But then you will have to go back to your constituents, to your electors, and educate them on what you were attempting to do. You have to educate them on what is to be expected. As advocates, you have to make sure that the particular interest of your electors, the people that elected you, are not forgotten in making the overall national plans.

I was fascinated this morning, when listening to this discussion of privatization, as to the variety of approaches to privatization. I would hope that as parliaments approach this vital question of privatization they would not forget, that no matter what variety of approach is taken, that it will move in the direction of certain well-established historical principles. I recall, for example, that the question of private property was one of the key aspects of the "Declaration of the Rights of Man and of Citizens" that was promulgated by the French national assembly in the year 1789. In Article 17 of the Declaration of the Rights of Man, property is referred to as "an inviolable and sacred right." So you are dealing, in this question of privatization, with more than just individual aspirations, you are dealing with one of the fundamental rights that has been developed over the centuries and is broadly recognized.

There is a related question of the control of monopolies. This, of course, is an extremely difficult question when dealing with economies which have been characterized by the existence of not one, but many monopolies; in fact, the whole series of monopolies that have been characteristic of a centralized economy.

I would give you just one example from the American experience. Until recently we had in the United States a gigantic monopoly in the communications industries. The American Telephone and Telegraph Company held virtually a total monopoly of all telephone service. It was finally concluded that this monopoly was not in the interest of the general public, not in the national interest, and so it was divided into a number of competing companies. Now before this breakup of AT&T, it required more than a year to fulfill an order by a customer for a high capacity circuit. Since the company has been divided into competing smaller companies, an order for a high capacity circuit now takes from 35 to 40 days to fill, an extraordinary difference in the response to public needs and public consumption.

It will fall upon your shoulders as parliamentarians to authorize entrance into international institutions. Some of you are already members of the International Monetary Fund, the World Bank and similar organizations. One thing that is important, in this respect, is to realize that these are not simply clubs to ornament your curricula vitae, these are serious organizations and they have a price for entrance that is not to be ignored. You have to understand what the terms of entering these institutions are, and I think you have to prepare your electors for the fact that they also pay a price. In some cases that price is a level of austerity, control of imports, and other economic controls which may be justified by the ultimate results, but can't be ignored as you enter into the process.

Earlier I said that it is not enough to enact laws, you have to oversee how they are administered. I would like to go back to that point for just a moment, because it seems to me it is a major parliamentary power. It ensures the correct interpretation of laws. It prevents corruption. It can be painful on occasion, but when it is painful, it is usually the moment when it is most effective. We had a very painful experience in the United States in the oversight of public affairs, and the event is known generally as

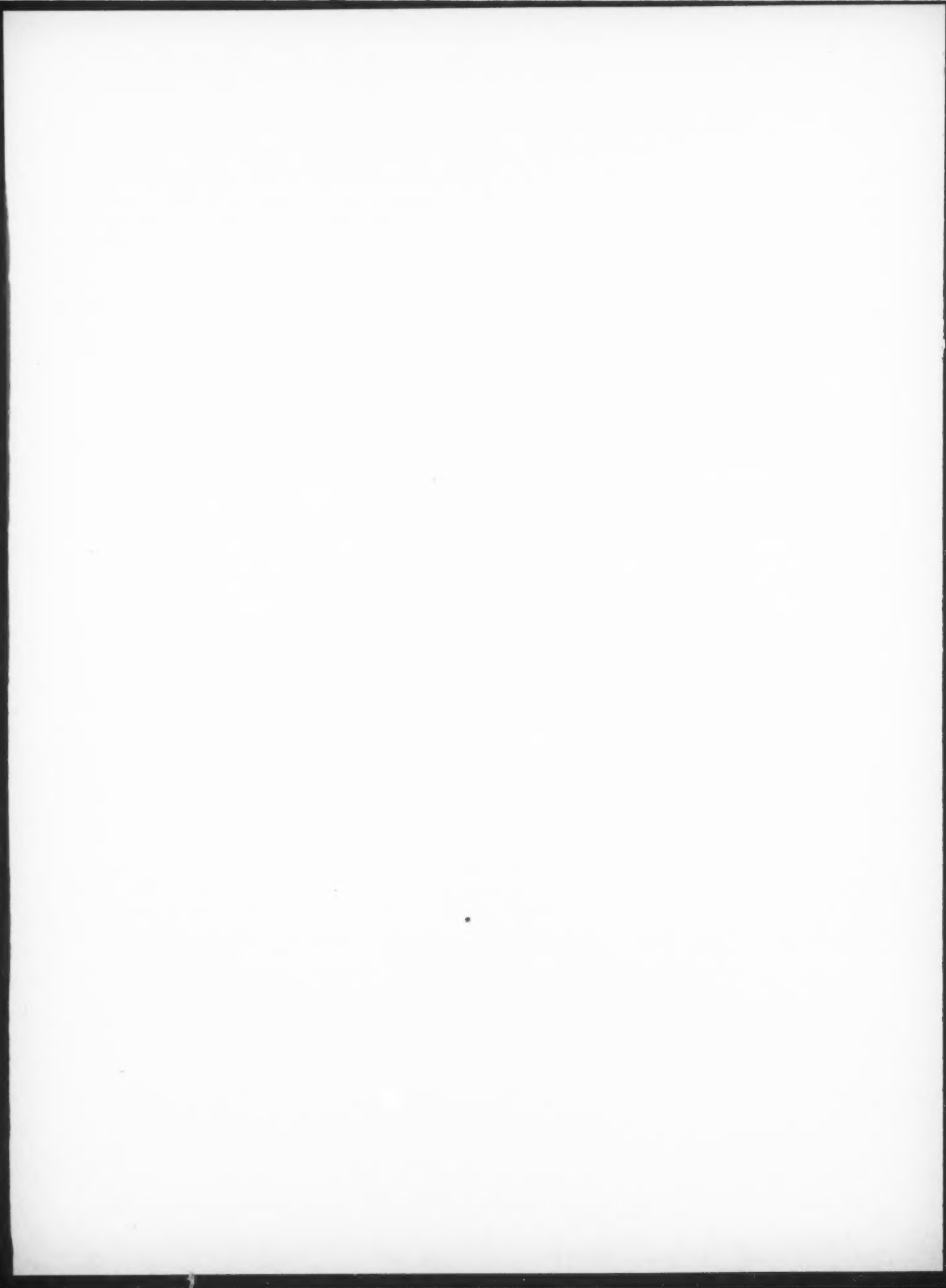
Watergate. I was a member of the Congress at that time and have very vivid memories of that experience. The very fact that parliamentarians had the duty and responsibility to oversee the administration of the laws made it possible to bring about corrections that were obviously necessary. Parliamentarians have the duty to establish the pace and the timing of reforms, and these are questions that cannot be delegated to economists, with all due respect to economists. These are duties that cannot be delegated to technocrats. You have to decide whether your case is suitable for shock treatment to the "quick fix", whether you ought to go for a slow process or moderate process.

You have to reach for comprehensive policies, policies that won't deal only with a section of your economy, but comprehensively with the total economy. In this decision you have to measure the human ability of your people to tolerate the cost of change. You have to be sure that there is a "safety net" to address the human aspects of political decisions. There was a wonderful old member of Congress from the State of Oklahoma named Paige Belcher. I remember when his constituents came to him with some complaints for which he had no answer, he said the only thing he could do was to put his foot up on the wagon tongue and cry with them. I am sure all of you have had similar decisions in your public lives. You know that the public perception must be that sacrifice is equitable, that it is fairly and equally shared by every single citizen, that it is sustainable, and that it will result in an improvement of the conditions of life in your country.

You have to make, of course, certain personal decisions about how you work. Some parliamentarians follow the peripatetic method, they simply are in constant motion doing everything everyday. Others follow the method of total immersion, deciding that one subject has priority for them and immersing themselves in that one subject to the exclusion of others. These are personal decisions, but in all of these decisions, I would hope that you would be aware of two pervasive issues that are inherent in every piece of legislation that you will address:

One is human rights, and second is the environment. And whether it is a banking bill, a bill for industrial reform, a bill for commercial transactions, or a bill for public works, you should assess its impact on these questions of human rights and on the environment, if you are, in fact, to be successful in achieving your legislative objectives.

APPENDICES



APPENDIX I: SEMINAR AGENDA

MARCH 21, THURSDAY

1600 Press Conference at Parliament

Tamás Szabó, Leader of Hungarian Parliamentary Delegation, Member of Parliament and Political State Secretary, Ministry of Finance

Daniel C. Matuszewski, Executive Director of The International Foundation

John P. Hardt, Associate Director, Congressional Research Service, U.S. Library of Congress

1900 Meeting of the Organizing Committee

MARCH 22, FRIDAY: MORNING SESSION

0830 Experts received by **Béla Kádár**, Minister for International Economic Relations, Hungary

0845 Parliamentary Leaders met by **György Szabad**, Speaker of the Hungarian National Assembly

0930 Formal Opening by Host Committee

Welcoming Remarks:

Tamás Szabó, Leader of Hungarian Parliamentary Delegation

György Szabad, Speaker of the Hungarian National Assembly

Daniel Matuszewski, Executive Director of The International Foundation

0945 Topic 1: Parliaments and Economic Development

Addresses:

"Separating Legislative, Executive and Judiciary Powers"

-**Árpád Göncz**, President of the Republic of Hungary

"The Parliament's Role in the Process of Establishing Market Oriented and Competitive Economies"

-**György Szabad**, Speaker of the Hungarian National Assembly

"Freedom and Prosperity - Are They Compatible?"

-**Helmuth Becker**, Vice President of the Bundestag

1030 Break

1045 **Topic 2: Democracy and Marketization**

Roundtable Discussion:

Chairpersons:

Mikolaj Kozakiewicz, President of the Sejm (Poland)

Daniel C. Matuszewski, Executive Director of The International
Foundation

Experts:

Francis T. Miko, Specialist on Soviet, Central, and East European Affairs,
Foreign Affairs and National Defense Division, Congressional Research
Service

Marvin R. Jackson, Director, The Leuven Institute for East European
Affairs

Parliamentarians:

Leaders of each Parliamentary Delegation - Introductory Remarks

AFTERNOON SESSION

1430 **Topic 3: Economic Programs for Transition to a Market Economy**

Addresses:

"The Responsibility and Limits of the Government in a Parliamentary
Democracy During the Transition to a Market Economy"

- **József Antall**, Prime Minister of the Republic of Hungary

"The Hungarian Government's Four-Year Program for Transition to a Market
Economy"

- **Tamás Szabó**, MP and Political State Secretary, Ministry for Finance

1500 Roundtable Discussion:

Chairpersons:

Dan Martian, President, Chamber of Deputies (Romania)

John P. Hardt, Associate Director, Congressional Research Service

Experts:

Anders Åslund, Director, Stockholm Institute of Soviet and East European Economics

Richard Judy, Director, Center for Soviet and Central European Studies, Hudson Institute

Parliamentarians:

Representatives of Economic and Budget Committees

1545 Break

1600 Roundtable resumes

MARCH 23, SATURDAY: MORNING SESSION

0830 Parliamentary Leaders meet with **President Árpád Göncz** in Munkácsy Hall, The House of Parliament

0830 Experts meet with **György Suranyi**, President, and **Imre Tarafás**, First Vice President of the National Bank of Hungary

0930 **Topic 4: Integration into the International Economy**

Address:

"Effective Integration Into the World Economy and the Role of International Institutions"

- **Béla Kádár**, Minister for International Economic Relations (Hungary)

0950 **Roundtable Discussion:**

Chairpersons:

Bogdana Glumac-Levakov, Speaker of the Federal Chamber of the National Assembly (Yugoslavia)

Harald Malmgren, Malmgren Associates

Experts:

David Bock, Director, Operations Staff, The World Bank

Val Koromzay, Director, Central and East European Division, Organization for Economic Cooperation and Development

György Szapáry, Assistant Director and Resident Representative, International Monetary Fund

Parliamentarians:

Specialists on international institutions and programs

1040 Break

1100 Roundtable resumes

1145 Address:

"The Helsinki Process and the Role of the Conference on Security and Cooperation in Europe in Transition"

- **Senator Dennis DeConcini**, Co-Chairman, U.S. Commission on Security and Cooperation in Europe (CSCE)

AFTERNOON SESSION

1430 **Topic 5: Trade and Investment**

Address:

"Technological Innovation - Its Importance in Economic Transformation and Modernization"

- **Erno Pungor**, Minister without Portfolio and President, National Committee for Technological Development (Hungary)

1500 Roundtable Discussion:

Chairpersons:

Nikolai T. Todorov, President of the Grand National Assembly (Bulgaria)

Charles Taylor, Executive Director, Group of Thirty, Consultative Group on International Economic and Monetary Affairs

Experts:

The Honorable Charles Vanik, Squire, Sanders & Dempsey and Former Representative, U.S. House of Representatives

Vera Trojan, Assistant Vice President, Wellington Management Company

John Williamson, Senior Fellow, Institute for International Economics

Marie Lavigne, Director, European Studies Center, Institute for East-West Security Studies

Jin-Hwan Chun, President and Chief Executive Officer, Lucky-Goldstar International

Parliamentarians:

Specialists on foreign trade, capital formation and foreign investment

1540 Break

1600 Roundtable Resumes

1700 Address:

"Preconditions for Economic Transition in Central and Eastern Europe"

- **George J. Vojta**, Executive Vice President, Bankers Trust Corporation

1800 Reception at the U.S. Ambassador's Residence hosted by the U.S. Commission on Security and Cooperation in Europe

Senator DeConcini, CoChairman of the Commission

Representative Helen Delich Bentley

Representative Robert K. Dornan

Representative Bob McEwen

Representative Bill Richardson

Representative E. Clay Shaw, Jr.

William D. Fritts, Jr., Department of Commerce

MARCH 24, SUNDAY: MORNING SESSION

0930 **Topic 6: Privatization**

"Privatization - A Key Process in the Establishment of a Free Market"

- **Andrei V. Orlov**, Deputy Chairman, USSR Cabinet of Ministers
Commission on Economic Reform (Soviet Union)
- **Lajos Csepi**, Managing Director, State Property Agency (Hungary)
- **Martin Miszerak**, Advisor to the Minister of Ownership Changes
(Poland)
- **Charles Jelinek-Francis**, Senior Advisor to the Minister of
Privatization of the Czech Republic (Czech and Slovak Federal
Republic)

1000 Roundtable Discussion:

Chairpersons:

František Mikloško, Speaker of the Slovak National Assembly (Czech and Slovak Federal Republic)

Michael Silverman, Squire, Sanders & Dempsey

Experts:

Anders Åslund, Director, Stockholm Institute of Soviet and East European Economics

Marvin Jackson, Director, The Leuven Institute for East European Studies

George Vojta, Executive Vice President, Bankers Trust Corporation

Parliamentarians:

Specialists on Privatization, Ownership Changes and Property

1040 Break

1100 Roundtable Resumes

1145 Address:

"Creation of a Legislative Agenda: Identification and Prioritization of Legislative Issues Involved in Economic Transformation"

- **Former Senator Charles McC. Mathias**, Vice Chairman of The International Foundation

AFTERNOON SESSION

1500 Topic 7: Monetary Stabilization

Addresses:

"Monetary Stabilization and Fiscal Policy - The Role of Central Banks"

- **Paul Volcker**, Chairman, James D. Wolfensohn Inc., and Former Chairman of the U.S. Federal Reserve

- **Frigyes Hárshegyí**, Deputy President of the National Bank of Hungary

Roundtable Discussion:

Chairpersons:

Yuri V. Blokhin, Deputy Chairman, Committee on Economic Reform USSR Supreme Soviet (U.S.S.R.)

Charles Taylor, Executive Director, Group of Thirty, Consultative Group on International Economic and Monetary Affairs

Experts:

Paul Volcker

Frigyes Harshegyi

Helmut Schlesinger, President-designate, Deutsche Bundesbank

Philippe Lagayette, First Deputy Governor, Banque de France

Jean-Jacques Rey, Deputy Governor, Bank of Belgium

Vukašin Marković, Vice President, Yugoslav National Bank

Viacheslav S. Zakharov, Deputy Chairman, U.S.S.R. State Bank

Sergei B. Fomin, Representative in Hungary, U.S.S.R. Bank for Foreign Economic Relations

György Szapáry, Assistant Director and Resident Representative, International Monetary Fund

1630 Closing Session - Conference Summation

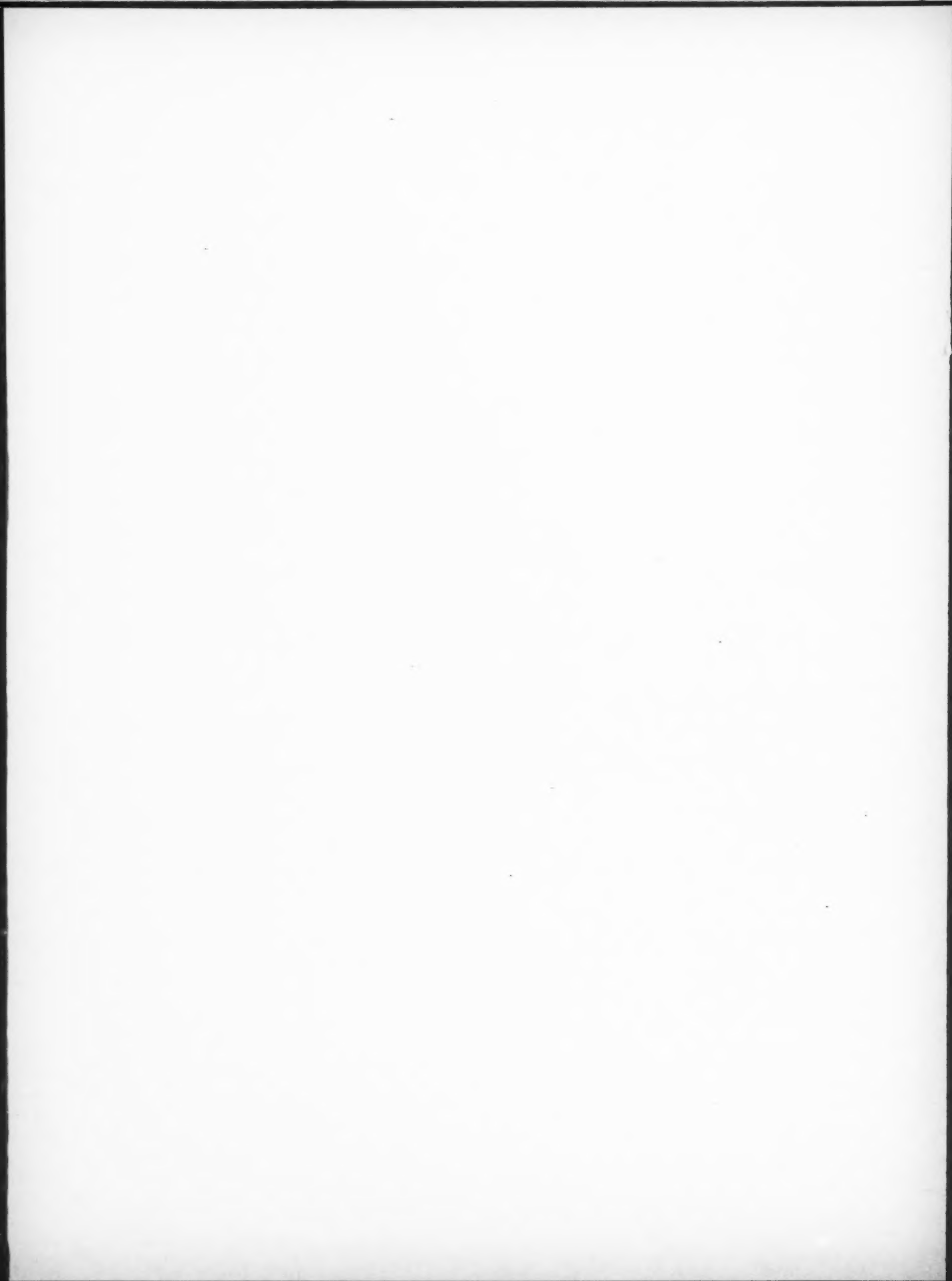
Charles McC. Mathias, Vice Chairman of The International Foundation

Alajos Dornbach, Deputy Speaker of the Hungarian National Assembly

1645 Seminar Adjourns

1700 Press Conference

Leaders of Parliamentary Delegations and Organizers



APPENDIX II: SEMINAR PARTICIPANTS

MEMBERS OF PARLIAMENT, GOVERNMENT OFFICIALS AND STAFF

I. Republic of Bulgaria

Nikolai T. Todorov
President, Grand National Assembly

Rumen M. Georgiev
Chairman of the Budget Committee, Grand National Assembly

Valentin Cerovszki
Member of Economic Commission, Grand National Assembly

II. Czech and Slovak Federal Republic (CSFR)

František Mikloško
Speaker, Slovak National Assembly

Ivan Carnogursky
First Vice President, Slovak National Assembly

Miroslav Tahy
Chairman, Economic Committee, House of Nations, CSFR Federal Assembly

Rudolf Zukal
Chairman, Economic Committee, House of the People, CSFR Federal Assembly

Libor Kudláček
Member, Economic Committee, House of the People, CSFR Federal Assembly

Charles Jelinek-Francis
Adviser to the Minister of Privatization of Czech Republic
Co-author of federal drafts of the CSFR laws of privatization

III. Federal Republic of Germany

Helmuth Becker
Vice President of the Bundestag

Paul Friedhof
Member of the Bundestag

Albert Probst
Member of the Bundestag

Fritz Schumann
Member of the Bundestag

Ernst Schwanhold
Member of the Bundestag

Albert Sepp
Bundestag Protocol

IV. Republic of Poland

Mikolaj Kozakiewicz
President of the Sejm

Andrzej Wielowiejski
Vice President of the Senate

Cezary Józefiak
Chairman, Senate National Economic Committee

Jan Raitar
Deputy Chairman, Sejm Foreign Affairs Committee

Krzysztof Pawlowski
Member, Senate National Economic Committee

Jerzy Rutecki
Member, Senate Foreign Affairs Committee

Martin A. Miszerak
Advisor to the Minister of Ownership Changes

Rafal Wisniewski
Senate Expert

Wladislaw Pulzon
Secretary of the Delegation

V. Romania

Dan Martian
President, Chamber of Deputies

Károly Kiraly
Vice President of the Senate

Ionel Blaga
Member, Chamber of Deputies
Chairman, Economic Committee

Ioan Bogdan
Member, Chamber of Deputies
Chairman, Budget and Finance Committee

Dragos Luchian
Chairman, Senate Financial, Banking and Budget Committee

Ferenc Salati
Expert

Romeo Oita
Staff to the President, Chamber of Deputies

Georghe Marinescu
Staff to the President, Chamber of Deputies

Alexandru Dobre
Staff to the President, Chamber of Deputies

Irina Bojin
Interpreter

VI. Union of Soviet Socialist Republics (USSR)

Yuri Vital'evich Blokhin
Deputy Chairman, Supreme Soviet Committee on Economic Reform

Konstantin Dmitrievich Lubenchenko
Deputy Chairman, Supreme Soviet Committee on Legislation

Nikolai Sergeevich Mironov
Member of Supreme Soviet Committee on Economic Reform
Director, Molniya, an industrial firm

Andrei V. Orlov
Deputy Minister, USSR Cabinet of Ministers
Deputy Chairman, State Commission for Economic Reform

Yevgeni P. Velikhov
Member, USSR Supreme Soviet
Vice President, Soviet Academy of Sciences
Chairman, The International Foundation

Viacheslav Sergeevich Zakharov
Deputy Chairman, USSR State Bank

Sergei B. Fomin
Representative in Hungary, USSR Bank for Foreign Economic Relations

Vladimir N. Sterlikov
Director, International Relations Department, USSR Bank for Foreign
Economic Relations (Moscow)

VII. United States

Senator Dennis DeConcini (D-Arizona)
Co-Chairman, U.S. Commission on Security and Cooperation in Europe
(CSCE)

Representative Helen Delich Bentley (R-Maryland)
Member of Congress

Representative Robert K. Dornan (R-California)
Member of Congress

Representative Bob McEwen (R-Ohio)
Member of Congress

Representative Bill Richardson (D-New Mexico)
Member of Congress
Member, U.S. CSCE

Representative E. Clay Shaw, Jr. (R-Florida)
Member of Congress

William D. Fritts, Jr.
Senior Advisor to the Secretary, Department of Commerce
Member, U.S. CSCE

Samuel G. Wise
Staff Director, U.S. CSCE

Jane S. Fisher
Deputy Staff Director, U.S. CSCE

David Evans
Senior Advisor, Soviet and East European Affairs, U.S. CSCE

Robert Hand
Staff Assistant, U.S. CSCE

Ronald McNamara
Staff Assistant, U.S. CSCE

Victoria Showalter
Staff Assistant, U.S. CSCE

Elez Biberaj
Interpreter, U.S. CSCE

Mary Hawkins
Legislative Director, Sen. DeConcini

June Tracy
Legislative Assistant, Sen. DeConcini

Stuart Nagurka
Press Secretary, Rep. Richardson

Eleanor Lewis
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